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Supreme Court, U.S.
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No. _____ OFFICE OF THE CLERK

In the Supreme Court of the United States

LEE M. TILL AND AMY M. TILL,
Petitioners,

v.

SCS CREDIT CORPORATION,
Respondent.

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

a) Is an undersecured creditor entitled to the "indubitable equivalent" of its nonbankruptcy entitlement for purposes of discounting deferred payments to present value under the Chapter 13 cramdown provision at 11 U.S.C. § 1325(a)(5)(B)(ii), resulting in fixing of a subprime lender's 21% contract rate as the presumptive discount rate?

b) What is the proper method for discounting of deferred payments to present value on property retained by the debtor under the Chapter 13 cramdown provision, and what is the creditor entitled to be compensated for in calculating the appropriate discount rate of interest?

PARTIES TO THE PROCEEDING

Petitioners

Petitioners Lee M. Till and Amy M. Till are individual citizens of the United States residing in the Southern District of Indiana. Neither Petitioner has corporate affiliations. Lee M. Till and Amy M. Till were the debtors in the Bankruptcy Court, the Appellees in the District Court and the Appellants in the Seventh Circuit Court of Appeals.

Respondent

Respondent SCS Credit Corporation is a corporation with no parent corporation. Petitioners are unaware of any publicly held company owning ten (10%) percent or more of said corporation's stock. SCS Credit Corporation was the objecting creditor in the Bankruptcy Court, the Appellant in the District Court, and the Appellee in the Seventh Circuit Court of Appeals.

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Petitioners respectfully petition for a Writ of Certiorari to review the opinion of the Seventh Circuit Court of Appeals in this case.

OPINIONS BELOW

The panel opinion of the United States Court of Appeals for the Seventh Circuit (App. B at 3a) was entered on August 21, 2002 and is reported at 301 F.3d 583 (7th Cir. 2002). The Order denying petition for rehearing *en banc* (App. A at 1a) was entered by the Seventh Circuit Court of Appeals on October 10, 2002 and is reported at 2002 U.S. App. LEXIS 21282 (7th Cir. 2002). The unreported opinion of the United States District Court for the Southern District of Indiana (App. C at 34a) was issued on November 1, 2000. The unreported order of the United States Bankruptcy Court for the Southern District of Indiana (App. D at 40a) was issued on June 27, 2000.

STATEMENT OF JURISDICTION

The opinion of the Seventh Circuit Court of Appeals was entered on August 21, 2002. The Court of Appeals entered an order denying a timely petition for rehearing *en banc* on October 10, 2002 (App. A at 1a).

The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTORY PROVISIONS INVOLVED

The operative statutory provision at 11 U.S.C. § 1325(a)(5) provides:[1]

> (a) Except as provided in subsection (b), the court shall confirm a plan if—
>
> * * * *
>
> (5) with respect to each allowed secured claim provided for by the plan—
>
> (A) the holder of such claim has accepted the plan;
>
> (B)(i) the plan provides that the holder of such claim retain the lien securing such claim; and
>
> (ii) the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim; or

[1] The critical "value, as of the effective date of the plan" language is commonly used as a term of art in the Bankruptcy Code. *See, e.g.*, 11 U.S.C. §§ 1325(a)(4), 1325(b)(1)(A), 1129(a)(7)(A)(ii), 1129(a)(7)(B), 1129(a)(9)(B)(i), 1129(a)(9)(C), 1129(b)(2)(A)(i)(II), 1129(b)(2)(B)(i), 1129(b)(2)(C)(i), 1225(a)(4), 1225(a)(5)(B)(ii), and 1225(b)(1)(A). These and other statutes are included at App. E to demonstrate the prevalence of the discounting to present value concept throughout the Code, and to illustrate the statutory context of the cramdown provision.

> (C) the debtor surrenders the property securing such claim to such holder; ...

STATEMENT OF THE CASE

Lee M. Till and Amy M. Till filed a petition for relief under Chapter 13, Title 11 of the United States Code on October 25, 1999. The underlying facts are not disputed. SCS Credit Corporation ("SCS") held a perfected security interest in the debtors' 1991 S-10 truck ("vehicle") retained by the debtors for personal use. The amount financed under SCS's original loan dated October 2, 1998 ("contract") was $6,425.00, with a total sale price of $8,385.24 (including interest at the rate of 21% per annum). The "cramdown" value of the vehicle was established by agreement at $4,000.00. The proposed three-year Chapter 13 plan provided for payments by wage assignment to the Trustee in the total amount of $740.00 per month. SCS's allowed secured claim was to be paid in full concurrently with payments on other allowed secured claims, with a discount factor of 9.5% to be paid on the declining balance of the $4,000.00 allowed secured claim from the date of confirmation (App. G at 77a-79a). The 9.5 % discount rate proposed by the debtors was based on a "formula method" (App. D at 43a) consisting of the prime rate as a base, with addition of a 1.5% risk premium ("prime-plus"). SCS objected to confirmation of the plan, arguing that, under the "coerced loan" method, SCS was entitled as a "subprime" lender to its 21% contract rate of interest to compensate for the return on its investment if it were permitted to foreclose on the vehicle and reinvest the proceeds in a like-kind loan (App. D at 41a).

The debtors' expert testified that standard lending institutions use the "prime rate" (national benchmark rate),

which not only accounts for the time-value of money ("a dollar now is a little more valuable that a dollar later"), but which also includes adjustment for the purchasing power of the dollar (the inflation rate), as well as risk and transaction costs. (App. F at 63a-64a).[2] SCS's expert testified that SCS does not sell vehicles on credit for a rate of interest less than 21%, and that 21% was the rate charged by other similar lenders in the area. (App. F at 73a). The Trustee recommended a formula method previously adopted by the courts in that district. (App. F at 60a-62a).

The Bankruptcy Court rejected the notion that the discount factor should be tied to the creditor's subprime lending status, and interpreted *Koopmans v. Farm Credit Services of Mid-America*, ACA, 102 F.3d 874 (7th Cir. 1996), to afford the court discretion to adopt the prime-plus 1.5% rate ultimately approved by the court. The matter before the Bankruptcy Court was a core proceeding within the meaning of 28 U.S.C. § 157(b)(2)(L). Exercising jurisdiction pursuant to 28 U.S.C. §§ 157(b)(1) and 1334, the Bankruptcy Court confirmed the amended Chapter 13 plan (App. D at 42a-43a).

SCS timely appealed the final order approving confirmation of the plan to the United States District Court for

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[2] This testimony is consistent with the common fact that the prime rate already includes a risk-cost premium to reflect the inherent risk in loans. Matthew Y. Harris, "Chapter 13 Cramdown Interest Rates: Another Day, Another Dollar--A Cry for Help in Ending the Quest for the Appropriate Rate," 67 Miss. L.J. 567, 581-82 (1997). It is for that reason that many courts and commentators prefer use of risk-free rates based on government securities, to which a risk premium may be added by the court. C. Frank Carbiener, "Present Value in Bankruptcy: The Search for an Appropriate Cramdown Discount Rate," 32 S.D.L.Rev. 42, 60-65 (1997).

the Southern District of Indiana, Indianapolis Division, which exercised jurisdiction pursuant to 28 U.S.C. §§ 158(a) and 1334. The District Court reversed the Bankruptcy Court on the basis that unrebutted evidence established that a "subprime" market existed and that the established rate for the subprime lending market was 21%, which the District Court considered the controlling inquiry under *Koopmans* (App. C at 38a). Under the District Court's ruling, the Bankruptcy Court erred as a matter of law and had no discretion to adopt the "prime plus" discount rate.

The debtors appealed the District Court decision to the Seventh Circuit. The majority panel of judges assigned to the case[3] interpreted *Koopmans* to mandate a "coerced loan" approach. Conceptualizing the cramdown process as forcing the creditor to extend a new line of credit to the debtor, the majority panel reasoned that "the creditor is entitled to the rate of interest it could have obtained had it foreclosed and reinvested the proceeds in loans of equivalent duration and risk," since nothing less would give the creditor the "indubitable equivalent" of its nonbankruptcy entitlement (App. B at 17a-18a). Adopting *GMAC v. Jones*, 999 F.2d 63 (3d Cir. 1993), the majority panel concluded that the "old contract rate will yield a rate sufficiently reflective of the value of the collateral at the time of the effectiveness of the plan to serve as a presumptive rate." (App. B at 20a).[4]

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[3] The panel decision was divided, with Judge Rovner (who had sat on the panel in *Koopmans*) issuing a rigorous 10-page dissent.

[4] The majority's non sequitur that the 21% contract rate is a "rate" presumptively "reflective of the value of the vehicle" at confirmation again demonstrates the majority's misapprehension of the purpose of the present value inquiry.

Tills timely petitioned for rehearing *en banc,* which was denied on October 10, 2002.

REASONS FOR GRANTING THE PETITION

Few other issues under the Bankruptcy Code have generated so many conflicting decisions and, in the words of the majority panel below, caused such "significant disagreement among the courts of appeals, bankruptcy courts and commentators." (App. B at 10a). The important federal question at issue is the standard to be applied in discounting deferred payments to "present value" under a Chapter 13 cramdown. Ten Circuits have now "become embroiled in the interest rate controversy," with each new decision "driving yet another wedge between the already split circuits." Matthew Y. Harris, "Chapter 13 Cram Down Interest Rates: Another Day, Another Dollar -- A Cry For Help in Ending the Quest for the Appropriate Rate," 67 Miss. L.J. 567, 568 (1997).

Disposition of the issue presented in this case can be expected to have a profound economic impact on bankruptcy jurisprudence nationwide. The legislature has expressed a clear intent to encourage filing of Chapter 13 reorganizations over Chapter 7 liquidations. H.R. Rep. No. 95-595, 95th Cong. 2d Sess.118, 129, *reprinted in* 1978 U.S. Code Cong. & Admin. News 5963, 6080, 6090. The impetus Congress intended for Chapter 13 is not yet reflected in the numbers. In 2001, 1,054,618 Chapter 7s were filed nationwide as compared to only 425,213 Chapter 13 filings. "Current Bankruptcy Statistics," http://www.abiworld.org/stats/currentstats.html. It is estimated that, like the debtors in the case below, nearly 60% of U.S. adults have "subprime" credit. "Sub Prime" Lending, 1998, 1999 New Media Auto Services, Inc., http://www.carinvoices.com/financing/about_financing/sub_prime_credit.htm. Analysts agree that "subprime" loans are "extremely profitable" for creditors,[5] Evan M. Gilreath, "The Entrance of Banks Into Subprime Lending: First Union and The Money Store," 3 N.C.Banking Inst. 149, n.18 (1999), resulting in great potential for abuse.

It is a fundamental purpose of Chapter 13 to provide all debtors with an effective means of retaining property and dealing with secured creditors. H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 124 (1977) *reprinted in* Vol. C, *Collier on Bankruptcy*, App. Pt. 4(d)(i) (Matthew Bender 15th ed. rev.). Yet few could disagree that financially-stressed debtors paying 21% interest under a Chapter 13 plan are *not* effectively dealing with their secured creditors — as the legislature intended. Most Chapter 13 plans are tightly budgeted, and reinstatement of the contractual interest rate will remove Chapter 13 as an option for many debtors based solely on their location of residence. [6] Under the same federal statute,

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[5] Subprime lending often involves financially unsophisticated borrowers desperate for credit who agree to unjustified high interest payments they cannot afford. Cathy Lesser Mansfield, "The Road to Subprime 'HEL' Was Paved With Good Congressional Intentions: Usury Deregulation and the Subprime Home Equity Market, 51 S.C.L. Rev. 473 (2000).

[6] Payment of an allowed secured claim in an amount of $15,000.00 at 9.5 % interest (the rate adopted by the Bankruptcy Court in the case below) over the maximum five-year plan term requires base funding in an amount of approx. $18,753.00 @ $312.55/month, whereas payment of $15,000.00 at 21 % interest over the same period requires base funding of $23,929.20 @ $398.82/month -- a staggering $5,176.20 increase in interest exclusive of the additional trustee fees generated thereon.

debtors in Indiana may be required to pay the contract rate of 21% or more, whereas debtors in a district applying a formula method may pay 7% -- contrary to the uniform application intended by Congress -- and perhaps the best evidence of misapplication of the present value concept which, if properly applied, could never produce such widely divergent results.

Nor do the implications of the lower court's ruling stop at 11 U.S.C. § 1325(a)(5)(B)(ii). The "value, as of the effective date of the plan" language appears in a variety of contexts throughout the reorganization chapters. Congress has expressed an intent that this language be read consistently to require discounting to present value wherever the term is used. Dean Pawlowic, "Entitlement to Interest Under the Bankruptcy Code, 12 Bankr. Dev. J. 149, 168-69 (1995). The absence of uniform standards has made the discount rate calculation "the most discussed and debated issue in Chapter 12 confirmation cases," where the present value language parallels that of Chapter 13. Scott L. Sanders, "Plan Confirmation Under Section 1225 of the Bankruptcy Code: Sowing the Seeds of Inconsistency," 8 Bankr. Dev. J. 291, 310 (1991).

The critical need for direction from this Court is evidenced on a daily basis in the form of protracted litigation depleting the limited time and resources of bankruptcy courts across the country. Matthew Y. Harris, "Chapter 13 Cram Down Interest Rates: Another Day, Another Dollar -- A Cry For Help in Ending the Quest for the Appropriate Rate," 67 Miss. L.J. 567, 583 (1997).

I. The Decision of the Seventh Circuit Court of Appeals Conflicts With the Decisions of Other Circuits

The majority panel's holding is squarely contrary to the decisions of the Second, Eighth and Ninth Circuit Courts of Appeals, all of which have adopted a "formula" method for computing the cramdown rate of interest. Under the "formula" method, the court adopts a readily-accessible or national risk-free rate as a base and adds a risk premium corresponding to the court's determination of the risk associated with the reorganization plan.

The Eighth Circuit in *United States v. Doud*, 869 F. 2d 1144, 1146 (8th Cir. 1989), was the first of the Circuits to approve a bankruptcy court's use of a "formula" approach in determining Chapter 12 cramdown interest (treasury bond plus 2% risk premium). The Ninth Circuit in *In re Fowler*, 903 F. 2d 694, 698 (9th Cir. 1990), concluded that the bankruptcy court had correctly adopted a "formula" approach (prime rate) for Chapter 12 cramdown, and remanded the case to the bankruptcy court for determination of an appropriate risk factor. The Second Circuit in *In re Valenti*, 105 F. 3d 55, 63 (2d Cir. 1997) [*modified on other grounds by Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997)], ruled that Chapter 13 cramdown interest should be fixed at the treasury bond rate plus a 1-3% risk premium.

II. The "Coerced Loan" Method is Fundamentally Flawed

Several other Circuits have applied variations of the "coerced loan" method adopted by the majority panel below. *Matter of Southern States Motor Inns, Inc.*, 709 F. 2d 647 (11th Cir. 1983), *cert.den*, 465 U.S. 1022 (1984); *United States v. Arnold*, 878 F. 2d 925 (6th Cir. 1989); *In re*

Hardzog, 901 F. 2d 858 (10th Cir. 1990); *United Carolina Bank v. Hall*, 993 F. 2d 1126 (4th Cir. 1993); *GMAC v. Jones*, 999 F. 2d 63 (3d Cir. 1993); and *In re Smithwick*, 121 F. 3d 211 (5th Cir. 1997), *cert. den.* 523 U.S. 1074 (1998). Yet even these Circuits cannot reach consensus. Whereas the Fourth Circuit in *United Carolina Bank*, 993 F. 2d at 1131, caps the discount rate at the contract amount, *GMAC v. Jones*, 999 F.2d at 70-71, and the majority panel below (App. B at 21a) recognize no such limit.

Petitioners contend that these cases are premised upon a series of errors that caused these Courts, like the majority below, to misapprehend the limited purpose of the present value calculation.

A. Improper Expansion of Plain Language of Statute

The majority panel begins with the premise that it is "reasonable to presume" what Congress intended under § 1325(a)(5) (App. B at 11a), and concludes that, "to exclude the element of profit from the fixing of the market rate would violate the statutory directive" that the creditor be placed in the same position that it would have been in had it been permitted to repossess the collateral (App. B at 19a). Remarkably, this so-called "statutory directive" appears nowhere in the statute.

The operative language of the Code is "value, as of the effective date of the plan" at 11 U.S.C. § 1325(a)(5)(B)(ii).

By the time the Bankruptcy Code was enacted, "present value" or the "time value of money" was recognized as a "term of art" in the financial community, meaning that a dollar received today is worth more than a dollar to be received in the future. Thus, a "discount rate" of interest is

applied to a stream of payments to ensure that the creditor will receive the same amount of money in the future that it would have received if there had been no delay in payment. E. Grant & W. Ireson, Principles of Engineering Economy 40 (4th ed. 1964). The "discount rate" is universally understood to consist of two components: 1) a riskless rate to account for the time value of money, and 2) an adjustment to account for risk. Richard A. Brealey and Steward C. Myers, Principles of Corporate Finance, p. 244 (6th Cir. 2000).

Against this backdrop, "[a]lthough the Code itself offers no definition of ... present value in this context, the legislative history describes the mechanical process of determining present value in a manner consistent with the use of the term by the economic and financial community." Dean Pawlowic, "Entitlement to Interest Under the Bankruptcy Code," 12 Bank. Dev. J. 149, 169 (1995). H.R. Rep. No. 95-595, U.S. Code Cong. & Admin. News 1978, p.6464 as appearing in 2 Appendix *Collier on Bankruptcy* at 408; H.R. Rep. No. 95-595, 95th Cong., 1st Sess., 414-15 (1977).

This Court in *Case v. Los Angeles Lumber Products Co., LTD.*, 308 U.S. 106, 115 (1939) adhered to the familiar rule of construction that "where words are employed in an act which had at the time a well known meaning ..., they are used in that sense...." The transformation of the historic present value concept into the creditor-specific inquiry undertaken by the majority could not occur without the specific intent of Congress clearly expressed in the statute, *Midlantic Nat'l Bank v. New Jersey Dep't of Envtl. Protection*, 474 U.S. 494, 501 (1986), and the language of the cramdown statute conveys no such intent.

It follows that a "plain language" interpretation of the statute suggests "a simple payment stream discounted to

reflect the time value of money in the current economy without any additional fact-based considerations." Michael E.S. Frankel, "The Emerging Fixed Cramdown Rate Regime: A Market-Driven Argument for Effective Fixed Rates in Bankruptcy Cramdown," 2 U. Chi. L. Sch. Roundtable 643 n. 75 (1995). It is the sole purpose of the discount to preserve the present value of a "claim" in a fixed amount--not to restore the creditor's entitlement under its pre-petition "loan."

These concepts are so well-accepted that the court in *In re Oaks Partners, LTD*, 135 B.R. 440, 445 (Bankr. N.D. Ga. 1991) noted that, because of the mechanical nature of the "present value" calculation, the *"time value of money"* approach is commonly referred to as the *"formula"* approach.

B. Misapplication of Legislative History

Congress has consistently described the obligation to pay "plan" or "present value" interest in very different terms than the obligation to pay pre-confirmation or "pendency" interest.[7] Despite the absence of any requirement for payment of "contractual" interest at § 1325(a)(5)(B)(ii), courts rejecting the formula method frequently conclude that there exists a "presumption" for the contract rate under § 1325(a)(5)(B)(ii).

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[7] Cf. 11 U.S.C. § 506(b) (App. E at 46a), where the Code refers to pre-confirmation "interest" on oversecured claims, and certain other charges "provided for under the agreement," and 11 U.S.C. § 726(a)(5) (App. E at 47a), where the Code refers to payment of "interest at the legal rate."

In the preeminent "coerced loan" case adopted by the majority below, the Court in *GMAC v. Jones*, *supra*, explained the presumption in favor of the contract rate as follows:

> There is, in the legislative history,...support for the idea that the contract rate is to be accorded...privileged significance when determining the appropriate interest rate. In the discussion of § 502(b).., the drafters noted that 'bankruptcy operates as the acceleration of the principal amount of all claims against the debtor. One unarticulated reason for this is that the *discounting factor for claims after the commencement of the case is equivalent to contractual interest rate on the claim.'* Bankruptcy Reform Act of 1978, P.L. 95-598, 1978 U.S. Code Cong.& Admin.News, 5849 (emphasis added).

999 F.2d at 70, n. 10.

The earliest "contract presumption" cases concluded from the above legislative history that "[o]f course, there is a presumption that the discount rate and the rate set forth in the contract are equivalent." *Matter of Smith*, 4 B.R. 12 (Bankr. E.D. N.Y. 1980); *Accord*, *Matter of Rogers*, 6 B.R. 472, 475 (Bankr. S.D. Ia. 1980)[noting that "Congress has suggested that there should be a presumption that a proper discount rate would be the same as the rate set out in the parties' interest bearing agreement"].

So it turns out that *GMAC v. Jones,* expressly adopted by the majority panel, had a pre-existing bias for the contract rate based upon misreference to legislative history of §

502(b). One commentator characterized this common misuse of the legislative history as follows:

> ...Congress pointed out section 502 required that ... any claim for unmatured interest be disallowed. [ ] The Reports also state that creditors' claims for amounts owing after the petition is filed must be discounted at a rate equal to the contract interest rate. [ ] In fact, the Reports went so far as to state that when discounting such claims, there is an 'irrebuttable presumption that the discount rate and the contractual interest rate (even a zero interest rate) are equivalent.' [ ] This language, however, has no relevance to the cramdown discount rate under sections 1129 and 1325.... And nowhere in the legislative history of sections 1129 or 1325 did Congress state that the deferred payment discount rate, which compensates for the time value of money, is equal to the contract rate.

C. Frank Carbiener, "Present Value in Bankruptcy: the Search for an Appropriate Cramdown Discount Rate," 32 S.D. L. Rev. 42 (1987) (citations omitted).

The fact that Congress considered but deliberately chose *not* to equate the present value discount rate to the contract rate is apparent from a review of the legislative process leading to the Bankruptcy Amendment and Federal Judgeship Act of 1984, where Congress specifically considered an amendment requiring the contract rate of interest to be paid under § 1325(a)(5)(B)(ii) and rejected it. H.R. 1085, 98th Cong., 1st Sess. § 19(2)(A) (1983); H.R. 1169, 98th Cong., 1st Sess. § 19(2)(A) (1983); H.R. 4786, 97th

Cong. § 19(2)(A) (1981).

C. Reliance Upon Unsupported and Conflicting Excerpts from Collier Treatise

The legislative history of § 502 is not the only false start that gave root to the "coerced loan" theory adopted by the panel majority.

Much of the confusion that has surrounded the § 1325(a)(5)(B)(ii) present value concept was generated by an editor's comment in the Collier Bankruptcy treatise, where it was submitted in the context of ascertaining present value for purposes of 11 U.S.C. § 1129(a)(9)(C), that "deferred payment" of an obligation under a plan is a "coerced loan" for which the creditor must receive a "market rate" of interest corresponding to the rate the creditor would charge to a third party in a like-kind loan. 4 Collier on Bankruptcy, ¶ 1129.03, at 1129-62, 63 (15th ed. 1987).

As described by the court in *In re Computer Optics, Inc.*, 126 B.R. 664, 671 (Bank. D.N.H. 1991), "without citing any ... authority ..., the Collier treatise took a 'quantum leap' from the present value concept (...time value of money) into a totally different concept of a loan transaction" involving a fact-specific inquiry that has "skewed the analysis ever since."

Ironically, when addressing the appropriate discount rate for purposes of *Chapter 13 cramdown*, the above Collier treatise adopted the "cost of funds" approach (App. B at 13a-15a), whereby the discount rate is set at the rate the creditor would have to pay to borrow the amount equal to the allowed secured claim. In harshly criticizing courts' attempts to apply the contract rate for the present value calculation under §

1325(a)(5)(B)(ii) despite the legislature's express rejection of the contract rate, the Collier treatise stated as follows:

> Thus, *contrary to the holdings of a number of courts, it is rarely appropriate to select the rate charged to the debtor in the original transaction as the present value discount rate*. Treating the chapter 13 deferral of payments like a new loan transaction, as those courts have done, provides the holder of the allowed secured claim with not only the cost of the funds it would lend but also the costs of the new loan transaction, which would not be incurred, and the profit that would be earned in that transaction. Neither of these latter two amounts would be received if the collateral were surrendered; .... To include them in the present value discount rate would give the holder of an allowed secured claim more than the equivalent of immediate payment of that claim in full.

5 Collier on Bankruptcy ¶ 1325.06, at 1325-37, 38 (15th ed. 1987) (emphasis added).[8]

[8] Ironically, the higher the original contract interest rate, the higher the costs saved by the creditor in bankruptcy. C. Frank Carbiener, "Present Value in Bankruptcy: The Search for An Appropriate Cramdown Discount Rate, 32 S.D.L. Rev. 42, 56 (1987), pp. 56-65.

D. Improper Invocation of *Murel* "Indubitable Equivalent" Doctrine

The final major source of "authority" for advocates of the "coerced loan" theory is the case of *In re Murel Holding Corp.*, 75 F. 2d 941 (2d Cir. 1935), which arose under the Bankruptcy Act of 1898 and introduced the concept of "indubitable equivalence."[9]

In *Murel*, the secured creditor held a mortgage on an apartment house. After the debtors defaulted on the mortgage, the creditor attempted to foreclose. The debtors obtained a stay of foreclosure and proposed a plan of reorganization to pay the creditor interest over 10 years, with full payment of the principal due at the end of the 10-year period, and no payment on principal or substitution of collateral in the interim. On appeal, the creditor complained that its interests were not "adequately protected." Judge Hand anticipated rejection of this "wholly speculative" plan, since the creditor would receive neither the principal, the

[9] The "indubitable equivalence" standard was never codified under Chapter 13, but was instead codified at § 1129(b). As an alternative to the Chapter 11 debtor's payment of "present value" as of the effective date of the plan under § 1129(b)(2)(A)(i)(II), the debtor can instead provide the "indubitable equivalent" of the creditor's secured claim under § 1129(b)(2)(A)(iii). The legislative history states that abandonment of the collateral to the class would satisfy this "indubitable equivalent" standard, as would a replacement lien on similar collateral. 124 *Cong. Rec.* H. 11,103, 11,104 (daily ed. Sept. 28, 1978) (remarks of Rep. Don Edwards); 124 *Cong. Rec.* S. 17,420, 17,421 (daily ed. Oct. 6, 1978) (remarks of Sen. DeConcini). The inapplicability of the "indubitable equivalent" concept to deferred payments under Chapter 13 cramdown is readily apparent.

property, nor an equivalent substitute for a period of 10 years. The Court thus found that treatment of the secured claim was insufficient to justify a stay of foreclosure. 75 F.2d at 942.

Misapplication of the *Murel* decision played a most decisive role in the erroneous conclusion ultimately reached by the majority below. The majority panel concluded that its application of the coerced loan approach was mandated by the Seventh Circuit decision of *Koopmans v. Farm Credit Serv. of Mid-America, ACA*, 102 F.3d 874 (7th Cir. 1996). *Koopmans* construed *Murel* as controlling precedent on the "rate of interest" that a secured creditor is to receive under a Chapter 12 cramdown. According to *Koopmans*, *Murel* mandated that a creditor in cramdown receive compensation for the "indubitable equivalence" of its property interest, which could only be achieved by the fixing of a market rate of interest that will make the creditor as well off in the reorganization as if the creditor had been permitted to foreclose its collateral and reinvest the proceeds in loans of equivalent duration and risk. 102 F.2d at 874-875. The panel majority read *Koopmans* and *Murel* together to compel a "coerced loan" approach whereby the creditor realizes the "indubitable equivalent" of its nonbankruptcy entitlement (App. B at 17a).[10] The fact that the cramdown statute did not even exist at the time of the *Murel* decision shows that the *majority panel would have reached precisely the same result*

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[10] In the dissent below, Judge Rovner noted that *Koopmans* has been interpreted as endorsing the formula, coerced loan and cost of funds approach, and can be best described as not requiring bankruptcy courts to use any particular approach (App. B at 31a). The Seventh Circuit in *Koopmans* expressly noted that it was not even "implying [that the method used by the bankruptcy court] is the only way to approximate the market rate of interest...." 102 F.3d at 875.

without the cramdown statute. The cramdown statute was unnecessary to the majority's analysis, and simply played no part in the outcome.

The precedential value placed upon *Murel* in the § 1325(a)(5)(B)(ii) context had been widely criticized, until it was finally dispelled by the *Murel* analysis undertaken by this Court in *United States Ass'n v. Timbers of Inwood Forest Assocs., LTD.*, 484 U.S. 365 (1988). This Court in *Timbers* made the critical distinction that Judge Hand in *Murel* used the words "indubitable equivalence" not with reference to **"interest"** (as it was interpreted by the Seventh Circuit in *Koopmans* and by the majority panel below), but rather "with specific reference to the **jeopardized principal** of its loan" (emphasis added). As explained by this Court in *Timbers*, whereas "interest" was assured under the plan in *Murel*, the plan made no provision for amortization of principal or maintenance of the collateral's value during the 10-year term. 484 U.S. at 378. *Murel* did not even involve the distribution of periodic deferred payments on principal -- the typical mode of payment under a Chapter 13 plan. Since the plan at issue in the present case provided for full payment of SCS's allowed secured claim (principal) with interest within the three-year plan term (App. G at 77a-78a), there was no "jeopardized principal" issue in the case below.[11] As noted by this Court in *Timbers*, *Murel* did proceed on the premise that the secured creditor is entitled to present value in the confirmation context, but the necessity for showing something more ("indubitable equivalence") in *Murel* resulted from the

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[11] It has been noted that even *Murel* would have permitted payment of the allowed value of the secured creditor's lien. Theodore Eisenberg, "The Undersecured Creditor in Reorganizations and the Nature of the Security," 38 Vand. L. Rev. 931,954 (1985).

plan's lack of proper provision for payment of the principal--*not from use of an insufficent present value discount rate*. 484 U.S. at 378. Contrary to the holdings of *Koopmans* and the majority below, *Murel* does *not* stand for the proposition that "indubitable equivalence" is to be used as a standard for calculating the cramdown interest rate. The central premise upon which the panel majority's decision was based -- that discounting to present value requires the undersecured creditor to receive the "indubitable equivalent" of its nonbankruptcy entitlement and be placed in as good a position as it would have been had it been entitled to foreclose its collateral and reinvest the proceeds -- derives not from the cramdown statute, but from a misapplication of the *Murel* doctrine -- and nothing more.

III. THE DECISION OF THE SEVENTH CIRCUIT COURT OF APPEALS CONFLICTS WITH THE DECISIONS OF THIS COURT

Although this Court has never addressed the precise issue presented in this case, the reasoning of several key decisions of this Court is contrary to the conclusion of the panel majority.

Pursuant to 11 U.S.C. § 1322(b)(2), Chapter 13 debtors can modify the rights of secured creditors such as SCS. This Court in *Nobleman v. American Savings Bank*, 508 U.S. 324, 329 (1993) determined that the "rights" implicated by § 1322(b)(2) are *those rights provided by state law*. One such "right" identified by *Nobelman* is the *contractual interest rate*. *Nobleman* established that a creditor's state-law property rights are recognized in bankruptcy *only* in the absence of controlling federal law. Chapter 13 "cramdown" by definition does not require creditor consent. *In re Milham*, 141 F. 3d 420, 425 (2d Cir.

1998), *cert. den.*, 525 U.S. 872 (1998). The "very essence" of § 1325(a)(5)(B)(ii) is *contract modification*. *In re Paschen*, 296 F.3d 1203 (11th Cir. 2002) (*pet. cert.* 10/8/02).

This Court in *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997), held that secured property retained by the debtor over the creditor's objection under § 1325(a)(5)(B)(ii) is to be valued at its present replacement value, based upon the § 506(a) mandate that value is to be determined in light of the proposed disposition of the property. This Court in *Rash* noted that the debtor under § 1325(a)(5)(B)(ii) is required to provide the creditor with payments, over the life of the plan, that will total the "present value" of the "allowed secured claim," i.e., the "present value of the collateral ...." 520 U.S. at 953. Although this Court in *Rash* did not address the method for computing present value, because *Rash* also centered on the "cramdown" provision, the lessons of *Rash* are many.

In *Rash*, this Court made clear that, by allowing Chapter 13 debtors to retain collateral over the secured creditor's objection, the Bankruptcy Code deliberately "reshaped debtor and creditor rights in a marked departure from state law." Further, the "Code's cram down option displaces a secured creditor's state-law right to obtain immediate foreclosure upon a debtor's default." Because this Court in *Rash* recognized the cramdown provision as "controlling federal law," this Court, unlike the majority panel below, easily rejected the argument that the creditor should be placed in the same economic position that it would have been had it exercised its state-court foreclosure rights. Under *Rash*, a creditor's "interest in property" is valued independent of its right to immediate possession of the collateral on default.

The *Rash* decision has several implications at odds with the "coerced loan" approach adopted by *GMAC v. Jones* and the majority panel. As noted by the Court in *In re Segura*, 218 B.R. 166 (Bankr. N.D. Ok. 1998):

> The *Jones* theory ... has at its core the assumption that the creditor would reinvest the *proceeds of liquidated collateral*. *Rash*, however, requires that the present value of the sum representing the replacement value of the collateral, rather than the liquidation value, be paid out over the life of the chapter 13 plan. *Id*. Since *Rash*, the *Jones* rationale rests upon a faulty premise and is unfairly advantageous to the creditor.

In re Segura, 218 B.R. 166, 173-74 (Bankr. N.D. Ok. 1998).

This Court in *Rash* noted that "[a]djustments in the interest rate do not fully offset" the "risks" of debtor default and property deterioration incurred by the creditor when the debtor retains the collateral, whereas "the replacement-value standard accurately gauges these additional risks." 520 U.S. at 158. The court in *In re Goodyear*, 218 B.R. 718, 721 (Bankr. D. Vt. 1998) thus noted that *Rash* shifted compensation for the risk of default from the "interest" component to the "valuation" component, and concluded that, "[i]f the risks ... occasioned by a debtor's retention and use of the collateral are 'accurately gauged' in the valuation process, then there is no occasion to provide additional compensation for the same risk in determining the appropriate interest

rate."[12]

The case of *United States Ass'n of Texas v. Timbers of Inwood Forest Assocs., LTD.*, 484 U.S. 365, 372 (1988) involved an undersecured creditor's request for pre-confirmation adequate protection payments pursuant to 11 U.S.C. § 362(d)(1) to result in realization of the "indubitable equivalent" of the creditor's interest in property under 11 U.S.C. § 361(3). This Court in *Timbers* determined that a creditor's "interest in property" means its security interest (value of collateral or allowed secured claim) without taking into account the creditor's state-law right to immediate possession of the collateral on default or lost opportunity costs resulting from the creditor's inability to liquidate the collateral pending confirmation of a Chapter 11 plan.

Distilled to its barest essence, the "coerced loan" theory adopted by the majority panel is an argument for compensating the creditor for "lost opportunity costs" which result when the creditor is denied the ability to immediately liquidate the collateral and reinvest the proceeds. *In re Collins*, 167 B.R. 842, 845-46 (Bankr. E. D. Tx. 1994). Under the language of the cramdown statute, the creditor is to be compensated *only* for the *fixed amount of the allowed secured claim* (an amount strictly limited to the value of the property securing the debt). As a result of the *Timbers'* strict adherence to the terms of the statute in defining the

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[12] In the dissent below, Judge Rovner concluded that by requiring the debtor to pay the creditor the (higher) replacement cost of the vehicle, "the Supreme Court has already ensured that the creditor will be afforded significant compensation for the risk of non-payment." (App. B at 30a.) All other Circuit decisions adopting the "coerced loan" approach, with the exception of the decision in *Smithwick*, 121 F.3d 211 (5th Cir. 1997), pre-dated the *Rash* decision.

undersecured creditor's property interest which must be adequately protected, *Timbers* has been read to remove the elements of profit and lost opportunity costs from the present value calculation.[13] Hon. John K. Pearson, "Ending the Judicial Snipe Hunt: The Search for the Cramdown Interest Rate," 4 Am. Bankr. Inst. L. Rev. 35, 52 (1996).

The *Timbers* analysis is also considered significant because "present value" under § 1325(a)(5)(B)(ii), much like adequate protection under § 362(d)(1), attempts to remedy the loss in value of money due solely to the passage of time (i.e., both serve to protect the status quo). *Timbers* rejected the notion that undersecured creditors should receive interest to compensate for lost opportunity costs before unsecured creditors had recovered any principal. 484 U.S. at 373.

This Court in *Timbers* concluded that only one meaning of "interest in property" produced a substantive effect compatible with the rest of the law without rendering portions of the statute a nullity. 484 U.S. at 371.

Similarly, in the present case, to reinstate the contract rate as the presumptive rate under § 1325(a)(5)(B)(ii) is, in the words of this Court, "to destroy the law under the pretext of enforcing it." *Earle v. Carson*, 188 U.S. 42, 47 (1903). By attempting to derive the interest rate without regard for the statutory framework of the cramdown provision, the majority panel has destroyed one of the most important contract modification rights afforded the debtor at § 1325(a)(5)(B)(ii).

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[13] Contrast the list of factors for which SCS was compensated by the panel majority, including profit (App. B at 19a), as well as compensation for depreciation in value of collateral and the creditor's cost of continuing to service the loan (App. B at 16a).

Critics of the "coerced loan" method also caution that the secured creditor could present expert testimony that no lender would make a loan which is compatible to the creditor's treatment under the proposed plan, only to propose an extreme rate of interest that a lender would require if it were to make such a loan, thus rendering the cramdown provision a "nullity." *In re River Village Assocs.*, 161 B.R. 127 (Bankr. E.D. Pa. 1993), *aff'd*, 181 B.R. 795 (E.D. Pa. 1995).

The "coerced loan" approach upsets the symmetry of the Code in other critical respects. 11 U.S.C. § 506(b) allows an oversecured creditor to add interest that accumulates prior to confirmation to the secured claim awaiting distribution under the debtor's plan. The post-petition interest under § 506(b) becomes part of the secured claim and may accrue until the effective date of the plan. Upon confirmation, § 1325(a)(5)(B)(ii) requires that payments made under the plan return the "present value" of the § 506(b) secured claim amount to the creditor. In the case of an oversecured creditor, §§ 506(b) and 1325(a)(5)(B)(ii) compliment each other and together ensure the full payment of the present value of the secured creditor's claim. *In re Harko*, 211 B.R. 116, 123 (2d Cir. BAP 1997), *aff'd*, 141 F. 3d 420 (2d Cir. 1998), *cert.den.*, 525 U.S. 872 (1998). As a result of the reference to the "agreement under which such claim arose" at § 506(b), the contract rate of interest has been recognized as a presumptive rate of interest under § 506(b). *In re Harko, supra*, 211 B.R. at 119. The substitution of a contract rate of interest for "present value" interest under § 1325(a)(5)(B)(ii) ignores the different objectives underlying the selection of the interest rates under these two sections. The Court in *In re Young*, 61 B.R. 150, 151-54 (Bankr. S.D. Ind. 1986) cited the case of *Matter of Burgess Wholesale Mfg. Opticians, Inc.*, 721 F.2d 1146 (7th Cir. 1983) as Seventh Circuit precedent to

distinguish statutory "present value" interest payments under § 1325(a)(4) and contractual interest under § 506(b).[14]

The majority panel's decision also redistributes rights between debtors and creditors contrary to the statutory scheme. The majority below adopted the holding of the Third Circuit in *GMAC v. Jones, supra*, 999 F. 2d 63, wherein the Court states as follows:

> Conversely, utilizing the same rebuttable presumption approach, if a debtor proposes a plan with a rate less than the contract rate, it would be appropriate, in the absence of a stipulation, for a *bankruptcy court to require the debtor to come forward with some evidence* that the creditor's current rate is less than the contract rate.

999 F. 2d at 70-71 (emphasis added).

Under 11 U.S.C. § 1325(a), the court "shall" confirm the plan if certain minimal requirements for confirmation are met. Under § 1325(a)(5)(A), the debtor need not satisfy § 1325(a)(5)(B) if the creditor fails to object to the plan. Requiring the debtor to "come forward with evidence" to support any below-contract interest rate renders § 1325(a)(5)(A) a nullity, and necessitates the setting of evidentiary hearings in Chapter 13 cases that, prior to the panel decision below, would have been routinely confirmed.

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[14] In their Petition for Rehearing *En Banc*, Petitioners asserted that the ruling of the majority panel below conflicted with the Seventh Circuit's earlier characterization of the "present value" calculation in *Burgess, supra*.

It is a well-recognized canon of construction that words repeated within the same statutory section have an identical meaning in the several places employed. *George Van Camp & Sons Co. v. American Can Co.*, 278 U.S. 245 (1929). The "value, as of the effective date of the plan" language appears throughout the reorganization chapters (App. E at 48a-54a), and has consistently been interpreted under a "present value" analysis to require that payments be adjusted "to allow for the changing value of a dollar". *See*, e.g., *United States v. Neal Pharmacal Co.*, 789 F. 2d 1283 (8th Cir. 1986) [method for determining proper discount rate is same under § 1129(a)(9)(C) for unsecured tax claims as § 1129(a)(7) for secured cramdown); *Accord*, *Matter of Burgess Wholesale Mfg. Opticians, Inc.* 721 F. 2d 1146, 1147 (7th Cir. 1983). In sharp contrast, under the majority panel's ruling, every unsecured claimant would be entitled to a different interest rate based on its contract or lending market when a debtor must pay "value, as of the effective date of the plan" to unsecured claimants to satisfy the best-interests-of-creditors test under § 1325(a)(4). Lundin, 2 Chapter 13 Bankruptcy § 112.1 at 112-8 (3d. ed. 2000).

Although this Court has never considered the appropriate discount rate in the context of the Bankruptcy Code, this Court has previously examined discounting to present value in other contexts. In *Commissioner of Internal Revenue* v. *National Alfalfa Dehydrating & Milling Co.*, 417 U.S. 134,150 (1974), this Court described the economics underlying "discount" to adjust for the difference between the interest prescribed in the *instrument* issued and the prevailing *market rate* for money, in much the same way the market rate concept was originally intended under the Code to distinguish "present value" plan interest from contract or pendency interest.

In the context of discounting lost future earnings to present value, this Court in *Jones & Laughlin Steel Corp. v. Pfeifer,* 462 U.S. 523, 537 (1983) concluded that the discount rate should be based on the rate of interest that would be earned on the "best and safest investments," and noted that the arithmetic necessary for discounting may be simplified through use of present value tables standard in the financial community. 462 U.S. at 537. This Court in *Pfeifer* concluded that federal law applied in determining the method for discounting to present value where the cause of action was rooted in federal maritime law. 462 U.S. at 547. Although these nonbankruptcy cases did not adopt an exclusive federal rule (for discounting award of future damages to present value), these cases applied terms employed by the financial and economic community to describe the limited function of the present value concept and to establish guidelines as to what factors could be considered and what losses must be excluded from the discounting process. To now redefine the present value concept in the bankruptcy context in the manner prescribed by the panel majority would be historically unprecedented.

IV. THE ISSUE HERE PRESENTED IS OF SUBSTANTIAL IMPORTANCE

The interest rate to be paid by debtors on claims existing at the time of reorganization is arguably "the most debated economic issue in bankruptcy litigation." Monica Hartman, "Selecting the Correct Cramdown Interest Rate in Chapter 11 and Chapter 13 Bankruptcies," 47 U.C.L.A. L. Rev. 521,522 (1999). Courts and commentators agree that the serious financial impact of the interest rate determination has made this issue the single-most contested issue in plan confirmation.

The decision of the panel majority requires that the creditor receive indubitable equivalence and lost opportunity costs rejected by this Court as part of the creditor's allowed secured claim, renders the § 1322 contract modification provision a nullity, and is patently unworkable within the statutory scheme of which § 1325(a)(5)(B)(ii) is a part.

The impact of the majority decision on the typical debtor can be devastating. The majority adopts rigid standards for confirmation in violation of the § 1325(a) mandate that the plan be confirmed if the minimal statutory requirements are met. Given the gross disparity between resources of debtors and creditors, overreaching creditors stand to profit immensely at the expense of unsecured creditors and the typical Chapter 13 debtor struggling to protect a family's most basic necessities.

Given the prevalence of the issue throughout the Code, the decision of the panel majority below can be expected to have unintended and irreversible consequences in all bankruptcy reorganization cases. Nor will the impact of the majority decision be remedied by bankruptcy reform, because the fundamental concept of discounting to present value will remain an historically central feature of the reorganization chapters. Given the sharp division amongst the Circuits and the urgent need for uniform standards, only a decision of this Court can address a problem of such national import.

CONCLUSION

Petitioners contend that numerous Circuits have applied the present value discount in a manner contrary to law. Both the "coerced loan" and the "presumptive contract" rates necessarily include profit and lost opportunity costs inapplicable to the present value discount. Absent misplaced

reliance on the *Murel* doctrine of indubitable equivalence, there simply exists no support in the Code or legislative history for the result reached by the majority below. The formula method conforms both with the language of the statute, and with the process by which "discounting" has been historically defined.

Petitioners request that this petition for certiorari be granted in order that this Court may establish national guidelines governing the discounting of deferred payments to present value in the bankruptcy context.

Respectfully Submitted,

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APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

No. 00-4167

[Filed October 10, 2002]

IN RE: LEE M. TILL and AMY M. TILL,
Debtors-Appellants.

Appeal from the United States District Court
for the Southern District of Indiana, Indianapolis Division
No. 00 C 1102
Larry J. McKinney, Chief Judge

JUDGES:
Before Hon. KENNETH F. RIPPLE, Circuit Judge, Hon. DANIEL A. MANION, Circuit Judge, Hon. ILANA DIAMOND ROVNER, Circuit Judge.

ORDER

Upon consideration of the Debtor-Appellants' petition for rehearing *en banc,* filed on September 3, 2002, no judge in active service has requested a vote thereon and the judges on the original panel have voted to deny the petition. Accordingly,

IT IS ORDERED that the petition for rehearing *en banc* is hereby DENIED.

APPENDIX B

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

No. 00-4167

[Argued April 10, 2002 - Decided August 21, 2002]

IN RE: LEE M. TILL and	)
AMY M. TILL,	)
Debtors-Appellants.	)
	)

Appeal from the United States District Court
for the Southern District of Indiana, Indianapolis Division
No. 00 C 1102
Larry J. McKinney, Chief Judge

JUDGES:
Before RIPPLE, MANION and ROVNER, Circuit Judges.
ROVNER, Circuit Judge, dissenting.

OPINION

RIPPLE, *Circuit Judge*. Lee and Amy Till filed for bankruptcy protection under Chapter 13. SCS Credit Corporation, a secured creditor, objected to confirmation of the Tills' Chapter 13 plan on the ground that the interest rate SCS would be paid under Chapter 13's "cramdown" provision, *see* 11 U.S.C. § 1325(a)(5)(A)(ii), was insufficient.

The bankruptcy court confirmed the plan over SCS' objection; it held that the proper interest rate was the prime rate plus a risk adjustment of 1.5%. SCS appealed. The district court reversed the bankruptcy court's decision; it concluded that the "coerced loan" theory applied, and, consequently, that the interest rate should be based on what SCS would receive for a loan of similar risk and duration. The district court stayed remand of its order pending the Tills' further appeal to this court. For the reasons set forth in the following opinion, we vacate the judgment of the district court and remand the case for further proceedings with instructions.

I

BACKGROUND

Lee and Amy Till jointly filed for bankruptcy protection under Chapter 13. SCS Credit Corporation was the only creditor to object to confirmation of the Tills' amended Chapter 13 plan. SCS is a secured creditor and holds a security interest in an automobile. The vehicle was valued at $ 4,500. SCS is a sub-prime lender, which means that it services borrowers with credit histories too poor to qualify for prime-rate auto loans. The Tills are such borrowers. The interest rate on the Tills' loan was 21%. The Tills' plan invoked the "cramdown" provision of Chapter 13.

Under Chapter 13's cramdown provision, a bankruptcy plan will be confirmed over the objection of a secured creditor if the creditor retains its lien on the collateral, and the creditor receives cash payments over the course of the plan that are equivalent to the value of the collateral on the plan's effective date. *See* 11 U.S.C. §

1325(a)(5)(B). To achieve this statutory requirement, the bankruptcy court must determine the value of the collateral, and the debtor must pay interest to account for the time value of money. Under the Tills' reorganization plan, the interest rate on SCS' secured claim would be 9.5%. SCS contended that this rate would not provide SCS with the present value of its collateral, as required by the cramdown provision. SCS submitted that the rate should be 21%, the interest rate it would have earned if SCS had foreclosed on the vehicle, sold it and then reinvested the proceeds in another sub-prime auto loan.

The bankruptcy court conducted a hearing to consider SCS' objection. The Tills presented the testimony of a finance professor who testified that an interest rate of 9.5%, which he based on the prime rate plus a risk premium of 1.5%, would be sufficient. He admitted, however, that he had no experience working for a creditor and only a limited understanding of the sub-prime auto lending market. SCS presented the testimony of its general manager, Neil Bird, and the sales manager of Instant Auto Finance, which had written the loan to the Tills and then had assigned it to SCS. Both witnesses testified that SCS had received 21% interest on all of its loans because borrowers like the Tills are poor credit risks. Bird also testified that SCS usually did not get paid the full amount under Chapter 13 plans because the debtors often cannot fulfill their obligations under the plan.

The bankruptcy court interpreted our decision in *Koopmans v. Farm Credit Services of Mid-America*, 102 F.3d 874 (7th Cir. 1996), to endorse a prime rate plus a risk premium method of calculating the proper cramdown interest rate. The court rejected the "coerced loan" theory of the

cramdown provision advocated by SCS. Following what it believed to be the holding of *Koopmans*, the bankruptcy court confirmed the Tills' plan with an interest rate of 9.5% applied to SCS' claim.

SCS then appealed to the United States District Court for the Southern District of Indiana. SCS reasserted its argument that it was entitled to 21%, the rate it would earn on a loan if it had foreclosed on the collateral and then had used the proceeds to issue a new loan. The district court agreed. The court held that the bankruptcy court had misread *Koopmans* and that *Koopmans* required that SCS receive the interest rate it would have earned on a new loan financed by the proceeds from the sale of its collateral. Based on the record in the bankruptcy court, the district court concluded that 21% was the proper rate and accordingly reversed the bankruptcy court's decision. The Tills now appeal that decision to this court.

II

DISCUSSION

A.

The issue before us--the appropriate approach to determine the applicable interest rate under Chapter 13's cramdown provision--first presents us with a question of statutory interpretation. We review this question de novo. The application of that method to the particular facts of this case is reviewed for clear error. *See In re Smithwick*, 121 F.3d 211, 215 (5th Cir. 1997).

The Tills submit that we should reverse the district court and reinstate the bankruptcy court's decision. In their view, a "market formula" method, such as the one adopted by the bankruptcy court in this case, appropriately implements the statutory mandate. SCS, however, contends that the "coerced loan" method, adopted by several Courts of Appeals and by the district court in this case, more accurately reflects the statutory intent.

When a petition is filed under Chapter 13 of the Bankruptcy Code, a bankruptcy court confirms the plan if several conditions are met. *See* 11 U.S.C. § § 1325(a)(1)-(6).[1] For secured creditors, this provision offers three possible

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[1] The statute provides:

Except as provided in subsection (b), the court shall confirm a plan if --

(1) the plan complies with the provisions of this chapter and with the other applicable provisions of this title;

(2) any fee, charge, or amount required under chapter 123 title 28, or by the plan, to be paid before confirmation, has been paid;

(3) the plan has been proposed in good faith and not by any means forbidden by law;

(4) the value, as of the effective date of the plan, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 of this title on such date;

prerequisites to confirmation, one of which must be satisfied before a Chapter 13 plan can be confirmed. If the secured creditor consents, *see* 11 U.S.C. § 1325(a)(5)(A), or the debtor surrenders the collateral, *see id.* § 1325(a)(5)(C), or if the plan invokes 11 U.S.C. § 1325(a)(5)(B), known colloquially as Chapter 13's "cramdown" provision, a Chapter 13 plan will be confirmed, as long as the other conditions of confirmation are met. *See* Todd J. Zywicki, *Cramdown and the Code*, 19 T. Marshall L. Rev. 241, 242-43 (1994). The cramdown provision permits a bankruptcy court to confirm a debtor's Chapter 13 plan over a secured creditor's objection if "the plan provides that the holder of such claim retain the lien securing such claim; and the value,

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(5) with respect to each allowed secured claim provided for by the plan --

(A) the holder of such claim has accepted the plan;

(B)(i) the plan provides that the holder of such claim retain the lien securing such claim; and (ii) the value, as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim; or

(C) the debtor surrenders the property securing such claim to such holder; and

(6) the debtor will be able to make all payments under the plan and to comply with the plan.

11 U.S.C. § 1325(a).

as of the effective date of the plan, of property to be distributed under the plan on account of such claim is not less than the allowed amount of such claim." 11 U.S.C. § 1325(a)(5)(B).[2] Both Chapter 11, *see* 11 U.S.C. § 1129(b)(2)(A)(i)(II), and Chapter 12, *see* 11 U.S.C. § 1225(a)(5)(B)(ii), contain analogous cramdown provisions. Courts have considered all three provisions to be similar and have analyzed them interchangeably.[3]

Before a plan invoking the cramdown provision can be confirmed, a bankruptcy court must make two determinations.

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[2] The allowed amount of a secured creditor's claim is the value of the collateral. The Code divides a secured creditor's claim into two portions, a secured portion and an unsecured portion. The secured portion is equal to the value of the collateral (for undersecured creditors) on the plan's effective date, the unsecured portion is the amount of the debt still owed to the creditor over and above the value of the collateral. *See United States v. Ron Pair Enters.*, 489 U.S. 235, 239, 103 L. Ed. 2d 290, 109 S. Ct. 1026 (1989). With respect to this excess amount, the secured creditor is treated like an unsecured creditor. *See id.*

[3] *See, e.g., Koopmans v. Farm Credit Servs. of Mid-America, ACA*, 102 F.3d 874, 875 (7th Cir. 1996) (citing cases interpreting Chapter 13's cramdown provision in a Chapter 12 case); *In re Smithwick*, 121 F.3d 211, 213 (5th Cir. 1997) (describing the cramdown provisions of Chapter 11 and Chapter 12 as analogous and citing to Chapter 11 cramdown cases in Chapter 12 case); *In re Fowler*, 903 F.2d 694, 697 (9th Cir. 1990) (finding that analysis in Chapter 11 cramdown cases also applied to Chapter 12 case); *United States v. Arnold*, 878 F.2d 925, 928 (6th Cir. 1989) (finding cramdown provisions of Chapter 12 and Chapter 13 to be identical).

First, it must determine the value of the collateral as of the effective date of the plan. *See Assocs. CommercialCorp. v. Rash*, 520 U.S. 953, 960-62 (1997). Once that value is determined, the bankruptcy court must then decide upon a stream of payments over the course of the plan that will provide the creditor with "value . . . not less than the allowed amount of such claim." 11 U.S.C. § 1325(a)(5)(B)(ii). To compensate a secured creditor for its delay in receiving the value of the collateral, the creditor must receive interest to account for the time value of money. *See* John K. Pearson, et al., *Ending the Judicial Snipe Hunt: The Search for the Cramdown Interest Rate*, 4 Am. Bankr. Inst. L. Rev. 35, 36-38 (1996). Thus, the second determination a bankruptcy court must make is the rate of interest to be charged. This issue has caused significant disagreement among the courts of appeals, bankruptcy courts and commentators. *See* Monica Hartman, Comment, *Selecting the Correct Cramdown Interest Rate in Chapter 11 and Chapter 13 Bankruptcies*, 47 U.C.L.A.L. Rev. 521, 532-44 (1999) (discussing the dominant approaches and the criticism each has received); David G. Epstein, *Don't Go and Do Something Rash About Cram Down Interest Rates*, 49 Ala. L. Rev. 435, 443-59 (1998) (discussing the divisions among courts of appeal); Matthew Y. Harris, Comment, *Chapter 13 Cram Down Interest Rates, 67 Miss. L.J. 567, 569-80 (1997)* (discussing the current approaches and their critics).

B.

Our ultimate task is to ascertain the policy decision made by Congress in enacting this statutory provision. This task requires that we understand the command of the statute. We therefore begin, as we always must, with the text of the

statute. We focus on the plain wording of the provision before us and on the statutory structure of which that provision is a part.[4] Examining both the text of the cramdown provision and the structure of the statute, we think it is clear that Congress intended that, under § 1325(a)(5)(B)(ii), the secured creditor, who is being forced to accept the debtor's plan and to forfeit his right to foreclose and sell the collateral, is to be compensated for the diminution of his present interest in the collateral. In short, from the debtor's perspective, it is necessary to pay for the continued use of the collateral at a rate that will preserve the value of the creditor's interest.

In ascertaining the precise obligation of the debtor under the cramdown provision, it is helpful to compare its requirements to the other provisions of § 1325(a)(5) that offer alternative ways of protecting the interest of a secured creditor in a Chapter 13 plan. We think it is reasonable to presume that Congress intended that each of these options afford the secured debtor somewhat equivalent protection.

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[4] In the case of an ambiguity in the statute, we sometimes find helpful, as long as it is read with prudence and caution, the legislative history of the provision. Although we have no need to resort to this device here, we note in passing that it is not very helpful to the task at hand. The House Report accompanying the 1978 Bankruptcy Act states that "value as of the effective date of the plan . . . indicates that the promised payment under the plan must be discounted to present value as of the effective date of the plan. The discounting should be based only on the unpaid balance of the amount due under the plan, until that amount, including interest, is paid in full." H.R. Rep. 95-595 at 408, *reprinted in* 1978 U.S.C.C.A.N. 5963, 6364. The report does not address the appropriate method of calculating the interest rate.

Certainly, none of the three was designed to provide the debtor or the creditor with a windfall.

The three possibilities are straightforward: (1) a creditor consents to the plan; (2) the debtor turns over the collateral to the creditor; or (3) the debtor invokes the cramdown. A creditor will only consent if the plan adequately protects its interests. *See* Pearson, *supra*, at 49-50 (describing the efforts of creditors and debtors to come to an agreement to avoid bankruptcy litigation). If the creditor receives the collateral, then its rights under state law are vindicated and its contract with the debtor is fulfilled; in such a circumstance, the secured creditor's rights are not impaired by the Bankruptcy Code. The creditor may still seek the unsecured portion of its claim in bankruptcy, but it proceeds as an unsecured creditor and without the preference the Code gives to secured creditors. Given these two alternate modes of protection afforded by the statute, it is logical to conclude that the interest rate under the cramdown provision must put the creditor in a position reasonably equivalent to the position it would be in had it consented to the plan or had it received and then sold the collateral. There seems to be a consensus on this point among courts of appeal that have addressed this issue. All agree that the rate should compensate the creditor for its delay in receiving the value of the collateral. *See, e.g., Koopmans v. Farm Credit Servs. of Mid-America, ACA*, 102 F.3d 874, 874 (7th Cir. 1996); *In re Smithwick*, 121 F.3d 211, 214 (5th Cir. 1997); *In re Valenti*, 105 F.3d 55, 59-60 (2d Cir. 1997); *GMAC v. Jones*, 999 F.2d 63, 66-67 (3d Cir. 1993); *United Carolina Bank v. Hall*, 993 F.2d 1126, 1129-30 (4th Cir. 1993); *In re Fowler*, 903 F.2d 694, 696-97 (9th Cir. 1990); *In re Hardzog*, 901 F.2d 858, 859-60 (10th Cir. 1990); *United States v. Arnold*, 878 F.2d 925, 928-29 (6th

Cir. 1989). "If the debtor chooses to maintain possession of the secured collateral . . . then the debtor must compensate the creditor for the full value of the allowed secured claim." *In re Valenti*, 105 F.3d at 59.

C.

Despite the consensus on the objective of the statute, courts have developed divergent formulae for calculating the interest rate. Even here, however, there is consensus about a starting point. Courts agree that a "market" rate of interest should apply. *See Koopmans*, 102 F.3d at 874-75; *In re Smithwick*, 121 F.3d at 214; *In re Valenti*, 105 F.3d at 63; *GMAC*, 999 F.2d at 66-67; *United Carolina Bank*, 993 F.2d at 1129-30; *In re Fowler*, 903 F.2d 694, 697 (9th Cir. 1990); *In re Hardzog*, 901 F.2d at 859-60; *Arnold*, 878 F.2d at 927-28; *see also* Pearson, *supra* at 40-41; Epstein, *supra* at 443. There is disagreement, however, about what rate of interest will adequately ensure that the creditor receives full value of his secured claim.

1.

Under one approach, known as the "cost of funds method," the interest rate is set at the rate the creditor would have to pay to borrow the amount equal to the collateral's value. *See In re Valenti*, 105 F.3d at 64 (holding that, although cost of funds approach "more appropriately reflects the present value of a creditor's allowed claim," it is difficult to administer, and therefore the interest rate should be "fixed at the rate on a United States Treasury instrument with a maturity equivalent to the repayment schedule under the debtor's reorganization plan"); 8 Lawrence P. King et al.,

Collier on Bankruptcy, P 1325.06[3][B] (15th ed. 2001) (advocating cost of funds approach). No court of appeals has adopted the cost of funds method without further refinement. In *In re Valenti*, the Second Circuit expressed the view that this method was the best of the approaches employed by the various federal courts, but chose to adopt, for the sake of efficiency and ease of administration, a standard rate for all cramdown cases. *See In re Valenti*, 105 F.3d at 64. As we shall discuss in more detail later, under the Second Circuit approach, the Chapter 13 plan ought to set the interest rate at the rate for Treasury instruments with a maturity equivalent to the repayment schedule set forth in the plan of reorganization. This rate ought then to be adjusted to take into account the creditor's risk in not receiving the payments scheduled under the plan. *See id*. The cost of funds' approach is advocated by *Collier on Bankruptcy* and has been adopted by some bankruptcy and district courts.

The cost of funds method is not without its flaws. First, as the Ninth Circuit has observed, charging an interest rate equal to the creditor's borrowing rate forces the creditor to make a firm commitment to borrow (and repay) funds secured only by the risky stream of payments under the debtor's Chapter 13 plan and the creditor's continuing lien on a depreciating piece of collateral. *See In re Camino Real Landscape Maint. Contractors, Inc.*, 818 F.2d 1503, 1506 (9th Cir. 1987). Such a rate does not give the secured creditor value equivalent to his allowed claim. Second, "it is doubtful that the secured creditor has an unlimited supply of credit." Michael E.S. Frankel, *The Emerging Fixed Cramdown Rate Regime*, 2 U. Chi. L. Sch. Roundtable 643, 647 (1995). The cost of funds method presupposes that a creditor will opt to exhaust some of its own credit in order to replace the liquid

capital it would have received after foreclosure and sale. Many Chapter 13 creditors are not in a financial position to take on such a commitment and, consequently, the imposition of such terms on them would not afford them the full value of their secured interest and would deprive them of the protection of the cramdown provision. Third, the cost of funds approach is likely to provide a windfall to the debtor. As a practical matter, it allows the debtor to step into his creditor's shoes and pay interest for use of the collateral on the terms that he would enjoy if he were the secured creditor. This approach does not compensate the creditor for the risk that the Chapter 13 plan will fail and leave the creditor with only the remedy of foreclosure and sale of depreciated collateral.

A second approach, which is an adaption of the cost of funds method, is the formula method. The Second Circuit, *see In re Valenti*, 105 F.3d 55, 63 (2d Cir. 1997), has adopted the formula method; the Ninth Circuit, *see In re Fowler*, 903 F.2d 694, 698 (9th Cir. 1990), and Eighth Circuit, *see United States v. Doud*, 869 F.2d 1144, 1146 (8th Cir. 1989), have endorsed the formula method but have not adopted an exclusive, strict formula; instead those courts have vested significant discretion in the bankruptcy courts. "The formula approach requires the court to adopt a risk-free market rate as a base, and then add a risk premium corresponding to the court's determination of the riskiness of the reorganization plan." Pearson, *supra*, at 50. As we have noted earlier, the Second Circuit uses the "rate on a United States Treasury instrument with a maturity equivalent to the repayment schedule under the debtor's reorganization plan"

and a risk premium of one to three percent. *In re Valenti*, 105 F.3d at 64.

The formula method as adopted by our colleagues in the Second Circuit has the advantage of being clear and predictable. The base rate is readily ascertainable, and there is a small range of risk adjustment. We do not believe, however, that the formula approach necessarily will produce an interest rate that complies with the statutory requirement that the creditor receive "value . . . [which is] not less than the allowed amount of such claim" over the course of the plan. 11 U.S.C. § 1325(a)(5)(B)(ii). Congress sought to protect the secured creditor who is forced into the cramdown situation with protection against several factors: (1) the possibility that his continued credit to the now-bankrupt debtor would not be repaid; (2) the reality that the collateral will continue to depreciate either at the same rate as it has in the past or at a different rate, depending on the nature of the collateral and the prevailing market conditions; (3) the cost of continuing to service the loan in question. Congress left to the bankruptcy courts the task of ascertaining the appropriate rate which would protect against all of these factors. As this court noted in *Koopmans*, market participants may choose different methods of calculating the market rate of interest for the new situation precipitated by the debtor's invocation of the cramdown provision. *See Koopmans*, 102 F.3d at 875. There are a multitude of possible creditor/debtor relationships subject to the cramdown provision. Each presents its own risks; to adopt a standard interest rate with limited discretion vested in the bankruptcy court only to take into consideration the contingency of nonpayment would not necessarily fulfill the statutory command that the creditor be afforded the full value of his interest at the time the reorganization plan

becomes effective. The statutory provision necessarily leaves the particular questions of valuation to the informed discretion of the bankruptcy court. Our adoption of a rigid formula would unduly restrict that discretion. The statute contemplates a more particularized inquiry, and we are bound by Congress' policy choice in this regard.

3.

A third approach, and the one that we adopted in *Koopmans*, has been described as the "coerced loan" or the "forced loan" method. Courts taking this view conceptualize the cramdown provision as forcing creditors to extend a new line of credit to the debtor. Consequently, "the creditor is entitled to the rate of interest it could have obtained had it foreclosed and reinvested the proceeds in loans of equivalent duration and risk." *Koopmans*, 102 F.3d at 875. This approach views § 1325(a)(5)(B)(ii) as "seeking to put the secured creditor in an economic position equivalent to the one it would have occupied had it received the allowed secured amount immediately, thus terminating the relationship between the creditor and the debtor." *GMAC*, 999 F.2d at 66-67; *see also In re Smithwick*, 121 F.3d at 214.

Koopmans was decided under the cramdown provision of Chapter 12, which applies to family farms. *See Koopmans*, 102 F.3d at 874. We wrote that in a cramdown, "the secured creditor is entitled to the 'indubitable equivalence' of its property interest, which means a stream of payments including interest that adds up to the present value of its claim." *Id.* at 874 (quoting *In re Murel Holding Corp.*, 75 F.2d 941, 942 (2d Cir. 1935) (L. Hand, J.)). The question there, as here, is: "At what rate of interest will [the secured

creditor] be as well off in the reorganization as if it had been allowed to foreclose on and sell the [collateral]." *Id*. We held that "the creditor is entitled to the rate of interest it could have obtained had it foreclosed and reinvested the proceeds in loans of equivalent duration and risk." 102 F.3d at 875. We so held "without implying that 'prime-plus' is the only way to approximate the market rate of interest--for participants in the market may use other methods . . . ." *Id*.

Some courts, including the bankruptcy court in this case, have read our holding in *Koopmans* to endorse the formula method discussed above. It is true that we affirmed the decision of the bankruptcy court, which had:

> approximated *this* by starting with the prime rate of interest, which it found prevalent for new 20-year well-secured agricultural loans at the time, and adding 1.5 percent because it deemed this extension of credit more risky than the norm in light of the Koopmans' sorry repayment record. This produced a floating rate, 10.5 percent (9 percent +1.5 percent) at the time the bankruptcy court approved the plan.

Koopmans, 102 F.3d at 875 (emphasis added). However, "this" was the "market rate of interest, at the time of the hypothetical foreclosure, for loans of equivalent duration and risk." *Id*. at 874-75. In *Koopmans*, the forced loan approach produced a 10.5% interest rate based upon the prime rate plus a risk factor; this result was a realistic approximation of the interest rate that the creditor would have received on a new loan of the same duration and risk because the secured

creditor in *Koopmans* was oversecured, and the chosen rate was the one for well-secured agricultural loans. *See id*. at 874-75. *Koopmans* did not endorse a formula approach and should not be read to have endorsed such an approach. As we emphasized in *Koopmans*, "on *this* record, the market's approach is prime-plus." *Id*. at 875. It is clear that *Koopmans* did not adopt the prime-plus rate; it adopted the coerced loan method, the specific application of which led to the prime-plus rate. *See id*.

Only the Second Circuit has explicitly rejected the forced loan method. *See In re Valenti*, 105 F.3d at 64. The court in *Valenti* thought the coerced loan method inappropriate because it computes "'present value' to include the profit that the creditor would have generated had the creditor received the value of the collateral immediately." *Id*. at 63. The court elaborated: "The objective of § 1325(a)(5)(B)(ii) is to put the creditor in the same economic position that it would have been in had it received the value of its allowed claim immediately. The purpose is *not* to put the creditor in the same position that it would have been in had it arranged a 'new' loan." *Id*. at 64. The court also opined that "the value of the creditor's allowed claim does not include any degree of profit." *Id*. Like several other circuits, we respectfully decline to adopt this analysis. Like the Third Circuit, *see GMAC*, 999 F.2d at 69, and the Fifth Circuit, *see Smithwick*, 121 F.3d at 214, we believe that to exclude the element of profit from the fixing of the market rate would violate the statutory directive that the creditor be placed in the same position as the one in which it would have been if it had been allowed to end the lending relationship by repossessing the collateral.

By determining the rate that the creditor in question would obtain in making a new loan in the same industry to a debtor who is similarly situated, although not in bankruptcy, *see GMAC*, 999 F.2d at 67 n. 4, we acknowledge that we are approximating, not necessarily duplicating precisely, the present value of the collateral to the creditor as that statute requires. The continuation of the old contract rate to the bankrupt debtor under the supervision of the bankruptcy court will involve some risks that would not be incurred in a new loan to a debtor not in default and also result in some economies.[5] Nevertheless, like our colleagues in the Third Circuit, *see GMAC*, 999 F.2d at 68-69, and Fifth Circuit, *see Smithwick*, 121 F.3d at 214, we believe that the old contract rate will yield a rate sufficiently reflective of the value of the collateral at the time of the effectiveness of the plan to serve as a presumptive rate. Therefore,

> [i]n the absence of a stipulation regarding the creditor's current rate for a loan of similar

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[5] As the Third Circuit noted in *GMAC*, an extension of the old loan will not involve the usual initiation costs and the bankruptcy trustee will assume some, although not all of the monitoring functions that must be undertaken in the administration of the loan. Other "relational costs" will also be less. *See GMAC*, 999 F.2d at 68. On the other hand, the usual "equity cushion" accompanying loans of this sort may be absent in the case of a coerced extension. *See id.* "An equity cushion exists when the appraised value of the collateral is greater than the value of the loan." *Id.* In a free market, uncoerced by the cramdown provision, a lender might well insist on a sizable equity cushion that is missing here. In a free market, the lender of an extension also might insist on a higher rate.

> character, amount and duration, we believe it would be appropriate for bankruptcy courts to accept a plan utilizing the contract rate if the creditor fails to come forward with persuasive evidence that its current rate is in excess of the contract rate. Conversely, utilizing the same rebuttable presumption approach, if a debtor proposes a plan with a rate less than the contract rate, it would be appropriate for a bankruptcy court to require the debtor to come forward with some evidence that the creditor's current rate is less than the contract rate.

GMAC, 999 F.2d at 70-71. The approach we endorse today will, in most cases, provide the best approximation of the proper rate. Thus, the bankruptcy courts are vested with significant discretion in the application of the method described in this opinion.

The district court properly determined that our earlier decision in *Koopmans* determined that the correct approach in ascertaining the appropriate interest rate in a cramdown situation is the coerced loan approach. Nevertheless, because our decision today sufficiently elaborates on that methodology and gives further guidance to the bankruptcy courts on this matter, we believe that the best course is to remand the case to the district court with instructions that the judgment of the bankruptcy court be vacated and that further proceedings consistent with this opinion be held in the bankruptcy court. We believe that fairness requires that both parties be afforded an opportunity to address the factors that we have identified in this opinion and that the bankruptcy court be given the

opportunity to employ the methodology that we have set forth today.

Conclusion

Accordingly, the judgment of the district court is vacated and the case is remanded with instructions. The parties shall bear their own costs of this appeal.

VACATED and REMANDED

DISSENT

ROVNER, *Circuit Judge*, dissenting. My colleagues hold that section 1325(a)(5)(B)(ii) entitles a creditor to the same interest rate that it would charge on a new loan to someone who is situated similarly (except for the bankruptcy) to the debtor. By its own account, the interest rate that SCS charges its customers for sub-prime, used car loans is whatever the market will bear. *In re Till*, No. 99-13425-13, Transcript of Continued Hearings on Trustee's Motion to Dismiss, etc., at 34, 38 (Bankr. S.D. Ind. Feb. 29, 2000). In the Tills' case, that was an eye-popping 21 percent. Compelling a debtor to pay such a burdensome rate of interest diminishes the feasibility of the Chapter 13 plan, *see* § 1325(a)(6); C. Frank Carbiener, *Present Value in Bankruptcy: The Search for an Appropriate Cramdown Discount Rate*, 32 S.D.L. REV. 42, 43 (1987), reduces the likelihood that unsecured creditors will receive any remuneration, *see In re Scott*, 248 B.R. 786, 793 (Bankr. N.D. Ill. 2000), and is inconsistent with the fresh start that Chapter 13 was intended to provide to debtors, *see Local Loan Co. v. Hunt*, 292 U.S. 234, 244, 54 S. Ct. 695, 699, 78 L. Ed. 1230 (1934); H.

Rep. No. 95-595, at 117 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6078. First and foremost, however, I believe it is contrary to the language and purpose of the statute.

Chapter 13's "cram down" provision obligates the debtor over the life of the plan to pay his creditor an amount of money "not less than the allowed amount" of the claim. 11 U.S.C. § 1325(a)(5)(B)(ii). Of course, a claim can only be allowed to the extent that it is secured, *see* 11 U.S.C. § 506(a), and so, when the creditor is under-secured as SCS was, the "allowed amount" of the claim corresponds to the value of the collateral underlying the loan (here, the automobile), *id. See ante* at 6 n.2; *Associates Commercial Corp. v. Rash*, 520 U.S. 953, 961, 117 S. Ct. 1879, 1884-85, 138 L. Ed. 2d 148 (1997). This means that the debtor must commit to a stream of payments that ultimately will compensate the creditor for the present value of the collateral that the debtor has chosen to keep. *Ante* at 7. Furthermore, because the debtor will be paying the creditor for the collateral over the three-to five-year life of the plan, the statute obligates the debtor to pay interest to compensate the creditor for the delay. *E.g., G.M.A.C. v. Jones*, 999 F.2d 63, 66 (3d Cir. 1993); *United Carolina Bank v. Hall*, 993 F.2d 1126, 1129-30 (4th Cir. 1993); *In re Bellamy*, 962 F.2d 176, 185-86 (2d Cir. 1992), *abrogated on other grounds by Nobelman v. American Sav. Bank*, 508 U.S. 324, 113 S. Ct. 2106, 124 L. Ed. 2d 228 (1993). In this way, the statute recognizes the time value of money and attempts to place the creditor in the same position it would have been in had the debtor surrendered the collateral, enabling the creditor to liquidate it and reinvest the proceeds. *See Rash*, 520 U.S. at 962, 117 S. Ct. at 1885; *Hall*, 993 F.2d at 1130; *Jones*, 999

F.2d at 66. As for the rate of interest, courts are virtually unanimous in the view that the interest rate imposed under section 1325(a)(5)(B)(ii) should be a "market" rate. *Ante* at 10; Monica Hartman, Comment, *Selecting the Correct Cramdown Interest Rate in Chapter 11 and Chapter 13 Bankruptcies*, 47 UCLA L. REV. 521, 528 (1999); Matthew Y. Harris, Comment, *Chapter 13 Cram Down Interest Rates: Another Day, Another Dollar--A Cry for Help in Ending the Quest for the Appropriate Rate*, 67 MISS. L.J. 567, 569 (1997); Todd J. Zywicki, *Cramdown and the Code: Calculating Cramdown Interest Rates Under the Bankruptcy Code*, 19 T. MARSHALL L. REV. 241, 245 (1994). They are divided, however as to which among several market rates most fairly compensates the creditor for the delay in receiving the value of its collateral--the rate at which the creditor could borrow money to replace the collateral that the debtor has chosen to keep (the "cost of funds" approach), the prime rate or a U.S. Treasury rate adjusted upward for the risk of nonpayment (the "formula" approach), or the rate at which the creditor would make the same type of loan to someone like the debtor (the "coerced loan" approach).

The coerced loan approach that my colleagues embrace posits that the debtor's decision to keep the collateral in effect compels the creditor to extend a new loan to the debtor for the value of the collateral. *Ante* at 14; *see Jones*, 999 F.2d at 67, quoting *Memphis Bank & Trust Co. v. Whitman*, 692 F.2d 427, 429 (6th Cir. 1982); *In re Hardzog*, 901 F.2d 858, 860 (10th Cir. 1990). It further presumes that had the debtor instead surrendered the collateral, the creditor would have converted the collateral into cash and invested the money in the same type of loan that the debtor originally obtained--here, a sub-prime used car loan carrying a high rate

of interest. *See ante* at 14, citing *Koopmans v. Farm Credit Servs. of Mid-America, ACA*, 102 F.3d 874, 875 (7th Cir. 1996). Based on the notion that the debtor's retention of the collateral has deprived the creditor of this investment opportunity, the coerced loan camp reasons that the debtor must pay the same rate of interest the creditor could have earned had it loaned the amount of the collateral to someone else. *Ante* at 14.

The sole deprivation that can be charged to the debtor, however, is the retention of the collateral, not the investment that the creditor presumably would have made with the proceeds of that collateral. *See In re Valenti*, 105 F.3d 55, 63-64 (2nd Cir. 1997), *abrogated on other grounds by Rash*, 520 U.S. 953, 117 S. Ct. 1879, 138 L. Ed. 2d 148. Had the Tills elected to surrender the collateral, all that SCS would have received is a 1991 Chevrolet S-10 truck, not a new loan package. It would have been SCS' responsibility to sell the truck and then make a new loan with the proceeds of the sale; and, of course, there would have been costs associated with both of those transactions. *See Hall*, 993 F.2d at 1131; *see also Koopmans*, 102 F.3d at 874 (deeming the appropriate question to be "at what rate of interest will [the secured creditor] be as well off in the reorganization as if it had been allowed to foreclose on and sell the [collateral]"). Requiring the debtor to pay the creditor the same rate of interest that the creditor would charge on a new loan to another consumer thus over-compensates the creditor, because it fails to account for the costs that the creditor would incur in funding the new loan. *See* 8 COLLIER ON BANKRUPTCY, P 1325.06, p. 1325-35-36 (Lawrence P. King, et al., eds., 15th rev. ed. 2002); *In re Ivey*, 147 B.R. 109, 116 (M.D.N.C. 1992), *overruled by Hall*, 993 F.2d 1126.

In this respect, the costs of funds approach comes closer to recognizing the economic consequences of the debtor's decision to keep the collateral. *See Valenti*, 105 F.3d at 64. Strictly speaking, the debtor's retention of the collateral does not preclude the creditor from making a new loan, it simply deprives the creditor of an asset that the creditor could convert into money and use to fund the new loan. A straightforward way to account for that deprivation is to ask what it would cost the creditor to obtain the cash equivalent of the collateral from an alternative source. 8 COLLIER, P 1325.0606, p. 1325-35; *In re Benson*, 9 B.R. 854, 858 (Bankr. N.D. Ill. 1981); *see also* Carbiener, 32 S.D.L. REV. at 63 (noting that this is consistent with law's general approach to mitigation of damages). Assume, for example, that SCS could borrow the cash equivalent of the Tills' truck at an interest rate of 10 percent and then lend that money to another consumer at a rate of 21 percent. Under that scenario, the cost of the Tills' decision to keep the truck would not be the full 21 percent that SCS would earn on its investment in another consumer loan, but the 10 percent that SCS would have to pay to borrow the money it otherwise would have obtained by liquidating the truck. Critics of the cost of funds approach point out that a creditor is unlikely to have an unlimited supply of credit and that it may be impractical and unjust to expect the creditor to borrow the funds necessary to replace the collateral that the debtor has chosen to keep. *See ante* at 11-12; *Hall*, 993 F.2d at 1130. Whether the creditor can, will, or should borrow to replace the funds it otherwise would realize from the collateral is entirely beside the point, however. The task at hand is to decide what rate of interest will reasonably compensate the creditor for the delay in receiving the value of the collateral from the debtor. *See* Zywicki, 19 T. MARSHALL L. REV. at 257. The cost of

funds approach better approximates this rate by examining what it would cost the creditor to replace the collateral with money from another source.

The principal disadvantage of the cost of funds method is that it calls for an individualized inquiry that will burden the parties and the court and may lead to disparate results depending on an individual creditor's cost of borrowing. *Valenti*, 105 F.3d at 64; *Hardzog*, 901 F.2d at 860. Given the relatively small amounts of money that are involved in a Chapter 13 proceeding, any approach that invites litigation and adds to the cost of the proceeding is undesirable. *See* Carbiener, 32 S.D.L. REV. at 59-60. The rate that ought to prevail under section 1325(a)(5)(B)(ii) is one that is predictable to the parties, and thus readily susceptible to agreement between them without court intervention. *See* § 1325(a)(5)(A).

In those respects, a formulaic approach that employs as a base rate of interest an easily referenced rate like the prime rate or the rate on U.S. Treasury instruments, and which allows for modest enhancements to the base to account for the risk of nonpayment, is superior, and I would commend it to the court. *See Valenti*, 105 F.3d at 64; *United States v. Doud*, 869 F.2d 1144, 1145 (8th Cir. 1989); Carbiener, 32 S.D.L. REV. at 63-65. The Treasury rate and the prime rate are both easily ascertainable rates that spare the court and the parties of the need for a potentially time-consuming and expensive inquiry into prevailing market rates of interest available to either the debtor or creditor. Each reflects two of the three components of a market interest rate--expected inflation, and "real" interest. *See* Hartman, 47 UCLA L. REV. at 531. The prime rate also includes the third

component--the risk of nonpayment (*see id.*)--and in that sense may represent a better starting point than the Treasury rate. *See Koopmans, 102 F.3d at 875;* Hartman, 47 UCLA L. REV. at 545. At the same time, because the prime rate is available to only the most credit-worthy borrowers, its risk component is arguably too small to compensate the creditor for the risk of nonpayment by a Chapter 13 debtor. *See Koopmans*, 102 F.3d at 875. Either rate, in any event, can be adjusted upward to account for the greater risk of nonpayment by a debtor in bankruptcy. *Id.* Courts employing the formula approach recognize that enhancements of one hundred to three hundred basis points would normally suffice for this purpose. *E.g., Valenti*, 105 F.3d at 64. What level of enhancement is called for in the individual case is a question wisely left to the bankruptcy court, which is better situated to assess the risk of nonpayment and may adjust the rate accordingly without extensive evidentiary hearings. *See* Hartman, 47 UCLA L. REV. at 545-46; Harris, 67 MISS. L.J. at 582.[1]

The lower interest rate produced by the formula approach (or for that matter by the cost of funds approach)--seemingly piddling by comparison with the rate produced by

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[1] This is essentially the approach that the bankruptcy court followed here, albeit after hearing testimony as to the prime rate and the prevailing rates of interest in the market for automobile loans. *See In re Till*, No. 99-13425-FJO-13, Order Confirming Amended Plan (Bankr. S.D. Ind. June 27,2000). A formula approach that starts with an easily referenced prime or Treasury rate and calls for an enhancement commensurate with the risks posed by the debtor's reorganization plan would largely obviate the need for such testimony. *See* Hartman, 47 UCLA L. REV. at 546-47.

the coerced loan approach in a sub-prime loan case like this one--may at first blush appear inadequate to compensate the creditor for the costs that the involuntarily extended lending relationship imposes, including in particular the risk that the debtor will be unable to discharge his obligations under the reorganization plan. *See ante* at 13; *see also Jones*, 999 F.2d at 67, 68-69; *In re Camino Real Landscape Maintenance Contractors, Inc.*, 818 F.2d 1503, 1506 (9th Cir. 1987). But courts should consider the extent to which the creditor has already been compensated for this risk in the rate of interest that it charged to the debtor in return for the original loan. Sub-prime lenders charge exorbitant rates of interest precisely because there is a high risk that their borrowers will default on their loan obligations. *See* Kathleen C. Engel and Patricia A. McCoy, *A Tale of Three Markets: The Law and Economics of Predatory Lending*, 80 TEX. L. REV. 1255, 1265-66 (2002); Mavis W. Kennedy, *Don't Let Your Client Be Labeled a Predatory Lender*, 89 ILL. B.J. 595, 597 (2001). These lenders understand that a significant number of their borrowers will not make good on their obligations--may, in fact, end up in bankruptcy. Yet, they continue to make high-risk loans because the money they receive from nondefaulting borrowers is enough to offset that risk; they would not remain in business otherwise. In short, the high interest rate on the Tills' used car loan already accounted for the very possibility of bankruptcy (and with it, the Tills' ability to keep their truck rather than surrender it) that has come to pass. Awarding SCS a second risk premium pursuant to section 1325(a)(5)(B)(ii) may well be unnecessary and inappropriate.

Courts must also have in mind the ways in which bankruptcy law and procedure also work to compensate the creditor for the risk of nonpayment. Insofar as the typical

automobile loan is concerned, the manner in which the loan collateral is valued for purposes of the bankruptcy itself provides the creditor with substantial compensation. Because the automobile typically is the only collateral securing the loan, and because automobiles depreciate relatively quickly, the creditor typically finds itself under-secured. That brings into play section 506(a) of the Code, which, as I noted at the outset, limits the amount of the creditor's allowed secured claim to the value of the automobile itself. In *Rash*, however, the Supreme Court held that for purposes of section 506(a), that value is to be determined by asking not how much the *creditor* could be expected to realize upon foreclosure and liquidation of the collateral, but by how much the *debtor* would have to pay in order to replace the collateral. 520 U.S. at 965, 117 S. Ct. at 1886. As Chief Judge Wedoff has pointed out, the replacement value of an automobile to the debtor will normally be significantly higher than the wholesale value that the creditor typically could expect to realize if it repossessed and liquidated the vehicle. *Scott*, 248 B.R. at 792. So by requiring the debtor who keeps the collateral to pay his creditor an amount equal to the replacement cost of the vehicle, the Supreme Court has already ensured that the creditor will be afforded significant compensation for the risk of non-payment. *Id.; see also* David G. Epstein, *Don't Go and Do Something Rash About Cram Down Interest Rates*, 49 ALA. L. REV. 435, 455 n. 79 (1998). Consequently, "applying a rate of interest that fully reflects risk of nonpayment--like the contract rate in the present case--to a secured claim amount that already includes substantial 'risk protection' results in a windfall for the secured creditor, to the detriment of unsecured creditors." *Scott*, 248 B.R. at 792, 793. Other provisions of the Code also operate, albeit more modestly, to reduce the risk of non-

payment along with the costs occasioned by the debtor's election to retain the collateral: (1) Before confirming the Chapter 13 plan, the Bankruptcy Court must be convinced that it is feasible in the sense that the debtor has the resources to meet his obligations, § 1325(a)(6); (2) wage orders can be used to ensure that the debtor does not inadvertently miss payments; (3) unsecured debt can be reduced or restructured; and (4) collection costs to the creditor are eliminated, while administrative costs are borne primarily by the Chapter 13 trustee. *See In re Carson*, 227 B.R. 719, 724 (Bankr. S.D. Ind. 1998); *see also Jones*, 999 F.2d at 69 & n. 8; Carbiener, 32 S.D.L. Rev. at 60-62.

I believe that my colleagues are correct to read this court's opinion in *Koopmans* as a nod in the direction of the coerced loan theory that they have elected to adopt; still, *Koopmans* ought not to be viewed as dispositive of the question we decide today. *See* Epstein, 49 ALA. L. REV. at 454 ("[*Koopmans*] can better be described as a case . . . that does not require bankruptcy courts to use any particular approach to determine the market rate."); *Carson*, 227 B.R. at 721 n.5 (noting that *Koopmans* "does not fit neatly into any of the three categories"). Although the language of the *Koopmans* opinion endorses the coerced loan approach, 102 F.3d at 875, the decision actually affirms the bankruptcy court's decision to use the prime rate with an appropriate risk enhancement, *id*. Indeed, courts and commentators have had some difficulty deciding where in the ongoing debate over the appropriate interest rate *Koopmans* came down, as evidenced by the fact that we have been credited with endorsing all three of the major approaches. *See, e.g., In re Smithwick*, 121 F.3d 211, 214 (5th Cir. 1997) (construing *Koopmans* as adopting the coerced loan approach), *cert. denied*, 523 U.S. 1074, 118

S. Ct. 1516, 140 L. Ed. 2d 669 (1998); Epstein, 49 ALA. L. REV. at 454 (noting that *Koopmans* actually approved the bankruptcy court's use of the formula approach); Harris, 67 Miss. L.J. at 580 & n. 74 (construing *Koopmans* as approving cost of funds approach); Timothy D. Moratzka, *Chapter 13 Interest Rate Pegged to Treasury Rate in Second Circuit*, 1997 ABI JNL. LEXIS 259, 14 AM. BANKR. INST. J. 16, 16 (1997) (same). In truth, the consequences of the choice were modest in *Koopmans*, because the nature of the debt at issue in that Chapter 12 case (an over-secured farm mortgage) rendered the gap between the prime rate and the prevailing market rate for comparable agricultural loans small--indeed, once the bankruptcy court had enhanced the prime rate for additional risk, the two rates were roughly equivalent. *See* 102 F.3d at 875; *Koopmans v. Farm Credit Servs.*, 196 B.R. 425, 428 (N.D. Ind. 1996). By contrast, the disparity here (as in many other Chapter 13 cases involving sub-prime consumer loans) is dramatic, so that use of a market rate for a comparable consumer loan will have adverse consequences that we did not address in *Koopmans*.

The search for a "market" rate that will place the creditor in the same position that it would have been in had it been able to foreclose on the loan is in a sense futile, because given a choice, a creditor would almost always prefer to take possession of the collateral immediately rather than accept a stream of payments over time for the value of that collateral. *See Rash*, 520 U.S. at 962-63, 117 S. Ct. at 1885; *see also Ivey*, 147 B.R. at 117-18. That choice has been taken away from the creditor, however, by operation of a statute that aims to help the debtor by allowing him to keep an asset--like an automobile--which may be vital to his ability to generate income and attend to his family's day-to-day needs. Because

this situation is a creature of legislation rather than the market, the policy considerations reflected in the statute cannot be ignored. A creditor is entitled to interest sufficient to compensate it for the delay in receiving the value of the collateral securing the loan, and the rate at which interest is ordered must reflect the risk of non-payment. To some extent, as I have noted, SCS has already been compensated for that risk through the high rate of interest it originally charged the Tills and other borrowers like them; that rate took into account the very possibility of default that came to pass. To the extent that the Tills' retention of the truck imposes new risks on SCS, the valuation of collateral at its replacement cost provides a substantial cushion to account for those risks. Overcompensating the creditor by demanding that the debtor pay interest as high as the market for high-risk loans will bear greatly increases the burden on the debtor, and far from the fresh start that Chapter 13 was intended to give him, puts him back in the very situation that brought him into bankruptcy. That burden works to the detriment not only of the debtor, but to that of his other creditors, secured and unsecured.

I respectfully dissent.

A true Copy:

Teste:

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Clerk of the United States Court of Appeals for the Seventh Circuit

APPENDIX C

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

[Filed November 1, 2000]

RE:
SCS CREDIT CORPORATION,
APPELLANT

LEE M. TILL and AMY M. TILL,
APPELLEES

IP 00-1102-C-M/S
DISTRICT COURT CASE NO.

Presiding Judge Larry J. McKinney Magistrate Judge V. Sue Shields

IN RE
LEE M. TILL and AMY M. TILL,
DEBTORS

99-13425-FJO-13
BANKRUPTCY CASE NO.

ORDER

Appellant creditor, SCS Credit Corporation (hereinafter "SCS"), has appealed the confirmation of the Chapter 13 Plan of Appellees Lee and Amy Till. The only issue concerns the proper interest rate the Tills must pay SCS on SCS's secured claim. The Plan set the interest at prime plus 1.5% and SCS asserts that under Seventh Circuit precedent the interest should have been set at the market rate. At the hearing on the objection to the Plan, SCS asserted that the market rate is 21%.

In reviewing a decision of the Bankruptcy Court, this District Court acts time of the confirmation of the plan. The record from the hearing in the Bankruptcy Court contains the testimony of three individuals addressing the appropriate interest rate. The Lees called an economics professor and SCS called a representative of Instant-Auto Finance and the general manager of SCS.

Professor Russell discussed the prime rate, defining it generally as the Rate banks charge their most credit worthy corporate customers and pointed out that the prime rate is a uniform rate across the country. He discussed factors that help determine that rate. He shared with the court his views on the factors that determine interest rates in the market. He looked at the average new car loan interest rate. He concluded, after being directed to consider the present value of these loans, and taking into account all the factors he had discussed that a fair interest rate for the automobile loans in this case would be nine and one-half percent. It is important to note that he did not testify about the market rate of loans similar to the loans in question, nor did he claim any expertise in the market in non-prime rates on auto loans, nor did he deny that such a market existed.

Craig Cook testified to 13 years' experience in a market for automobile loans he referred to as the sub-prime or non-prime market. He testified that in any loan situation in which the borrower had the same or similar credit history as the debtors in this case, the Tills, the interest rate was 21%. He indicated that as far as he knew that interest rate was determined by a consideration of what the market will bear. Neal Bird, an employee of SCS, testified that he had worked in the non-prime lender loan market for 4 years after working in the prime lender market for 9 years. His experience was that borrowers agreed to the 21% rate charged by non-prime lenders. He also opined that the 21% interest rate was determined more by what the market will bear than by a formula that takes into amount risk, profit, marketing costs and collection cost. He denied having a degree in economics or being an actuary.

Bankruptcy Judge Otte cited the *Koopmans* case. He also cited cases decided by Bankruptcy Judges Bayt and Metz, both of which applied a prime plus interest rate in similar cram down auto loan cases. Judge Otte adopted the reasoning of those cases. No separate findings of fact were entered.

The unrebutted testimony in this case is that there is a market for used car loans called the non-prime or sub-prime market. The unrebutted testimony is that the interest rate in this market is set not by economic considerations such as risk, transactional costs, and overhead. The unrebutted testimony is that the interest rate is set on no other consideration than what the market will bear. Potential borrowers are in this non-prime market because their credit histories are poor and they are therefore risky debtors. Presumably these borrowers cannot find a lender in the prime market. Presumably no

reasonable borrower would pay 21% interest on a vehicle if other cheaper rates were an as appellate tribunal and is governed by traditional standards of appellate review. Specifically, the Court "is constrained to accept the Bankruptcy Court's findings of facts unless they are clearly erroneous." *In Re Excalibur Auto Corp.*, 859 F.2d 454, 457, n. 3 (7th Cir. 1988); *In Re Longardner & Associates, Inc.*, 855 F.2d 455, 459 (7th Cir. 1988). "A finding is clearly erroneous if upon review of the entire record the reviewing court is left with the definite and firm conviction that a mistake has been committed." *Graham v. Lennington*, 74 B.R. 693, 695 ((S.D. Ind. 1987). "Generally, as long as the bankruptcy judge's inferences are reasonable and supported by the evidence, they will not be disturbed." *Id.*

Conclusions of law made by the Bankruptcy Court, however, must be reviewed *de novo. Excalibur Auto Corp.*, 859 F.2d at 457, n. 3; *Longardner & Associates, Inc.*, 855 F.2d at 459; *In Re Bonnett*, No. 87-2102 slip op. at 3 (7th Cir. Dec. 20, 1989). And, where the challenged finding is a mixture of law and fact, the clearly erroneous standard is also inapplicable. *Graham*, 74 B.R. at 965. The determination of the correct interest rate to be applied in this case for the SCS loan is a factual determination.

In the Seventh Circuit after the case of *Koopmans v. Farm Credit Services of Mid-America, ACA*, 102 F.3d 874, 875 (7th Cir. 1996) the interest rate to be applied under the cramdown provisions of 11U.S.C. §1225(a)(5)(B)(ii) is the market rate for loans of equivalent duration and risk which was available at the available to them. The choice these borrowers have may seem unfair: pay 21% or have no transportation.

Koopmans requires the Bankruptcy Court in a cramdown circumstance to set the rate of interest at the level that the creditor "could have obtained had it obtained had it foreclosed and reinvested the proceeds in loans of equivalent duration and risk." at p. 875. Further, *Koopmans* warns, "The market rate must be used consistently." at. P.875. The controlling inquiries under *Koopmans* are whether there is a market for these loans and if there is what is the market rate. The answers to these inquiries, says *Koopmans*, will allow the court to factually determine what "rate of interest a creditor could have obtained had it foreclosed and reinvested the proceeds in loans of equivalent duration and risk." The controlling inquiry is not into the changed nature of the risk of a loan once it becomes a part of a Chapter 13 plan.

The unrebutted evidence deduced at the hearing on the creditor's objection to the plan establishes that a sub-prime market exists and that its rate is 21%. Thus the unrebutted evidence here is that had SCS foreclosed on the Tills, SCS would have obtained the 21% rate in a loan of equivalent duration and risk. Whether this 21% interest rate may be set arbitrarily or that it may seem to take advantage of debtors who find themselves with bad credit histories is not the controlling inquiry. The fact that the contract rate is 21% is not controlling for this Court's decision. Again, what is controlling is the market rate.

For the above reasons, the judgment of the Bankruptcy Court is REVERSED and the matter is remanded for further consideration of the debtors' plan consistent with this opinion.

IT IS SO ORDERED this 1st day of November, 2000.

/s/ _____
Larry J. McKinney, Judge
United States District Court
Southern District of Indiana

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APPENDIX D

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVI S ION

CASE NO.99-13425-FJO-13

[Filed June 27, 2000]

IN RE:	)
	)
LEE MADISON TILL	)
AMY HELEN TILL	)
Debtors	)
	)

ORDER CONFIRMING AMENDED PLAN

This matter came before the Court upon the filing of the Objection to Confirmation filed by SCS Credit Corp. The Court held a hearing on this matter on February 29, 2000. Subsequent to the hearing, the Debtors, SCS Credit Corp. and the Chapter 13 Trustee filed briefs or comments with the Court. This matter is now ready for the Court's consideration.

The Court, after reviewing this matter and having researched the relevant authorities, now makes the following entry.

Bankruptcy Court Order Confirming Amended Plan - 6/27/00

Summary of Facts

The indebtedness between the Debtors and SCS Credit Corp. ("SCS") is secured by a lien on a vehicle. The Debtors' Amended Plan provides for a 9.5% rate of interest to be paid to SCS on its indebtedness.

The creditor asserts that it is entitled to a 21% interest rate, which the creditor claims is the rate it would obtain if it foreclosed on the vehicle and reinvested the proceeds in loans of equivalent duration and risk as the loan made by the Debtors and the creditor. SCS asserts that the Debtors' amended plan fails to comply with the "present value" requirement.

The Debtors argue that this Court should not adopt the "coerced loan" approach as proposed by SCS. The Debtors encourage this Court to follow the line of cases which have found that the "objective of section 1325(a)(5)(B)(ii) is to put the creditor in the same economic position that it would have been in had it received the value of its allowed claim immediately", not to "put the creditor in the same position that it would have been in had it arranged a "new" loan." citing *In Re Valenti*, 105 F.3d 55, 64 (2nd Cir. 1997).

The Chapter 13 Trustee filed Comments with the Court asking the Court to uphold the 9.5% provided for by the Debtors in their Amended Plan for the following reasons: (i) it is easily ascertainable on a daily basis; (2) prime is a more general statement as to the condition of the financial market; (3) its use avoids increases/decreases in the interest rate that reflects the strengths or weaknesses of a particular

lender; (4) it resolves the problems inherent with the contract rate cases; (5) it is linked most directly to the real loss experienced by the creditor; and (6) it does not engage courts, debtors and creditors in the frustrating search for non-existent markets and non-existent "similar loans".

Legal Discussion

The Seventh Circuit dealt with this issue in *Koopmans v. Farm Credit Serv. of Mid-America, ACA*, 102 F.3d 874 (7th Cir. 1996). The Seventh Circuit affirmed the lower court's application of prime plus 1.5%. Judge Robert Bayt issued an opinion on October 1, 1998 dealing with the appropriate rate of interest to be included in the plan as to a secured lender on a vehicle. (*In re Carson*, 227 B.R. 719 (S.D. Ind. 1998). Judge Bayt, following *Koopman*, held that the appropriate rate of interest to meet the requirements of Section 1325(a) (5) (B) (ii) was prime plus 1.5%.

Judge Anthony Metz, in an unpublished opinion in *In re Pippins* (98-13561-AJM-13 dated February 17, 1999), addressed facts very similar to the ones before this Court. In *Pippins*, the same creditor, SCS Credit Corporation, filed an objection to the Plan that was the same objection that was filed in this case, wherein it asserts that the secured creditor is entitled to an interest rate of 21%. Judge Metz applied a 10% rate of interest which follows the same standard applied by Judge Bayt in *Carson* and by the Seventh Circuit in *Koopmans*.

This Court is not persuaded with the reasoning set forth in the unpublished memorandum decision (In the Matter

of Stahl-Karfomenos 93-33622) by Judge Dees on May 20, 1999 cited by SCS wherein he held that a non-prime creditor was entitled to receive 20.99% interest under a chapter 13 plan.

This Court adopts the "prime-plus" approach and holds that the appropriate rate of interest to be applied to SCS Credit Corporation's debt is 9.5%. Based upon the foregoing, this Court APPROVES. the confirmation of the Debtors' Amended Plan as filed and OVERRULES the Objection of SCS to the Amended Plan.

Date JUN 27 2000

/s/ _____
FRANK J. OTTE
BANKRUPTCY JUDGE

DISTRIBUTION:
Attorneys of Record
United States Trustee

APPENDIX E

RELEVANT STATUTES

SECTION 361 (11 U.S.C. § 361)

§ 361. Adequate protection.

When adequate protection is required under section 362, 363, or 364 of this title of an interest of an entity in property, such adequate protection may be provided by—

* * * *

(3) granting such other relief, other than entitling such entity to compensation allowable under section 503(b)(1) of this title as an administrative expense, as will result in the realization by such entity of the indubitable equivalent of such entity's interest in such property.

* * * *

SECTION 362 (11 U.S.C. § 362)

§ 362. Automatic stay.

(a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title, or an application filed under section 5(a)(3) of the Securities Investor Protection Act of 1970, operates as a stay, applicable to all entities, of—

* * * *

(d) On request of a party in interest and after notice and a hearing, the court shall grant relief from the stay provided under subsection (a) of this section, such as by terminating, annulling, modifying, or conditioning such stay–

(1) for cause, including the lack of adequate protection of an interest in property of such party in interest;

(2) with respect to a stay of an act against property under subsection (a) of this section, if—

(A) the debtor does not have an equity in such property; and

(B) such property is not necessary to an effective reorganization; or

* * * *

SECTION 502 (11 U.S.C. 502)

§ 502. Allowance of claims or interests.

* * * *

(b) Except as provided in subsections (e)(2), (f), (g), (h) and (i) of this section, if such objection to a claim is made, the court, after notice and a hearing, shall determine the amount of such claim in lawful currency of the United States as of the date of the filing of the petition, and shall allow such claim in such amount, except to the extent that—

* * * *

(2) such claim is for unmatured interest;

* * * *

SECTION 506 (11 U.S.C. § 506)

§ 506. Determination of secured status

(a) An allowed claim of a creditor secured by a lien on property in which the estate has an interest, or that is subject to setoff under section 553 of this title, is a secured claim to the extent of the value of such creditor's interest in the estate's interest in such property, or to the extent of the amount subject to setoff, as the case may be, and is an unsecured claim to the extent that the value of such creditor's interest or the amount so subject to set off is less than the amount of such allowed claim. Such value shall be determined in light of the purpose of the valuation and of the proposed disposition or use of such property, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest.

(b) To the extent that an allowed secured claim is secured by property the value of which, after any recovery under subsection (c) of this section, is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement under which such claim arose.

* * * *

SECTION 726 (11 U.S.C. § 726)

§ 726. Distribution of property of the estate

(a) Except as provided in section 510 of this title, property of the estate shall be distributed--

* * * *

(5) fifth, in payment of interest at the legal rate from the date of the filing of the petition, on any claim paid under paragraph (1), (2), (3), or (4) of this subsection; and

* * * *

SECTION 1129 (11U.S.C. § 1129)

§ 1129. Confirmation of plan

(a) The court shall confirm a plan only if all of the following requirements are met:

* * * *

(7) With respect to each impaired class of claims or interests--

(A) each holder of a claim or interest of such class--

(i) has accepted the plan; or

(ii) will receive or retain under the plan on account of such claim or interest property of a **value, as of the effective date of the plan**, that is not less than the amount that such holder would so receive or retain if the debtor were liquidated under chapter 7 of this title on such date; or

(B) if section 1111(b)(2) of this title applies to the claims of such class, each holder of a claim of such class will receive or retain under the plan an account of such claim property of a **value, as of the effective date of the plan**, that is not less than the value of such holder's interest in the estate's interest in the property that secures such claims.

* * * *

(9) Except to the extent that the holder of a particular claim has agreed to a different treatment of such claim, the plan provides that--

(A) with respect to a claim of a kind specified in section 507(a)(1) or 507(a)(2) of this title, on the effective date of the plan, the holder of such claim will receive on account of such claim cash equal to the allowed amount of such claim;

(B) with respect to a class of claims of a kind specified in section 507(a)(3), 507(a)(4), 507(a)(5), 507(a)(6), or 507(a)(7) of this title, each holder of a claim of such class will receive--

(i) if such class has accepted the plan, deferred cash payments of a **value, as of the effective date of the plan**, equal to the allowed amount of such claim; or (ii) if such class has not accepted the plan, cash on the effective date of the plan equal to the allowed amount of such claim; and

(C) with respect to a claim of a kind specified in section 507(a)(8) of this title, the holder of such claim will receive on account of such claim deferred cash payments, over a period not exceeding six years after the date of assessment of such claim, of a **value, as of the effective date of the plan**, equal to the allowed amount of such claim.

* * * *

(b) (1) Notwithstanding section 510(a) of this title, if all of the applicable requirements of subsection (a) of this section other than paragraph (8) are met with respect to a plan, the court, on request of the proponent of the plan, shall confirm the plan notwithstanding the requirements of such paragraph if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.

(2) For the purpose of this subsection, the condition that a plan be fair and equitable with respect to a class includes the following requirements:

(A) With respect to a class of secured claims, the plan provides--

(i)(I) that the holders of such claims retain the liens securing such claims, whether the property subject to such liens is retained by the debtor or transferred to another entity, to the extent of the allowed amount of such claims; and

(II) that each holder of a claim of such class receive on account of such claim deferred cash payments totaling at least the allowed amount of such claim, of a **value, as of the effective date of the plan**, of at least the value of such holder's interest in the estate's interest in such property;

(ii) for the sale, subject to section 363(k) of this title, of any property that is subject to the liens securing such claims, free and clear of such liens, with such liens to attach to the proceeds of such sale, and the treatment of such liens on proceeds under clause (i) or (iii) of this subparagraph; or

(iii) for the realization by such holders of the indubitable equivalent of such claims.

(B) With respect to a class of unsecured claims--

(i) the plan provides that each holder of a claim of such class receive or retain on account of such claim property of a **value, as of the effective date of the plan**, equal to the allowed amount of such claim; or

* * * *

(C) With respect to a class of interests--

(i) the plan provides that each holder of an interest of such class receive or retain on account of such interest property of a value, as of the effective date of the plan, equal to the greatest of the allowed amount of any fixed liquidation preference to which such holder is entitled, any fixed redemption price to which such holder is entitled, or the value of such interest; or

* * * *

§ 1225. Confirmation of plan

(a) Except as provided in subsection (b), the court shall confirm a plan if--

* * * *

(4) the **value, as of the effective date of the plan**, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 of this title on such date;

(5) with respect to each allowed secured claim provided for by the plan--

(A) the holder of such claim has accepted the plan;

(B) (i) the plan provides that the holder of such claim retain the lien securing such claim; and

(ii) the **value, as of the effective date of the plan**, of property to be distributed by the trustee or the debtor under the plan on account of such claim is not less than the allowed amount of such claim; or

(C) the debtor surrenders the property securing such claim to such holder; and

* * * *

(b) (1) If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, **as of the effective date of the plan–**

(A) the **value** of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or

* * * *

SECTION 1322 (11 U.S.C. § 1322)

§ 1322. Contents of plan.

* * * *

(b) Subject to subsections (a) and (c) of this section, the plan may—

* * * *

(2) modify the rights of holders of secured claims, other that a claim secured only by a security interest in real property that is the debtor's principal residence....

* * * *

SECTION 1325 (11 U.S.C. § 1325)

§ 1325. Confirmation of plan

(a) Except as provided in subsection (b), the court shall confirm a plan if--

(4) the **value, as of the effective date of the plan**, of property to be distributed under the plan on account of each allowed unsecured claim is not less than the amount that would be paid on such claim if the estate of the debtor were liquidated under chapter 7 of this title on such date;

(5) with respect to each allowed secured claim provided for by the plan--

(A) the holder of such claim has accepted the plan;

(B) (i) the plan provides that the holder of such claim retain the lien securing such claim; and

(ii) the **value, as of the effective date of the plan**, of property to be distributed under the plan on

account of such claim is not less than the allowed amount of such claim; or

(C) the debtor surrenders the property securing such claim to such holder; and

* * * *

(b) (1) If the trustee or the holder of an allowed unsecured claim objects to the confirmation of the plan, then the court may not approve the plan unless, **as of the effective date of the plan**--

(A) the **value** of the property to be distributed under the plan on account of such claim is not less than the amount of such claim; or

* * * *

TITLE 28, JUDICIARY AND JUDICIAL PROCEDURE

28 USCS § 157 (2002)

§ 157. Procedures

* * * *

(b) (1) Bankruptcy judges may hear and determine all cases under title 11 [11 USCS §§ 101 et seq.] and all core proceedings arising under title 11 [11 USCS §§ 101 et seq.], or arising in a case under title 11 [11 USCS §§ 101 et seq.], referred under subsection (a) of this section, and may enter

appropriate orders and judgments, subject to review under section 158 of this title [28 USCS § 158].

(2) Core proceedings include, but are not limited to--

* * * *

(L) confirmations of plans;

* * * *

28 USCS § 158 (2002)

§ 158. Appeals

(a) The district courts of the United States shall have jurisdiction to hear appeals[ ]

(1) from final judgments, orders, and decrees;

* * * *

28 USCS § 1254 (2002)

§ 1254. Courts of appeals; certiorari; certified questions

Cases in the courts of appeals may be reviewed by the Supreme Court by the following methods:

(1) By writ of certiorari granted upon the petition of any party to any civil or criminal case, before or after rendition of judgment or decree;

* * * *

28 USCS § 1334 (2002)

§ 1334. Bankruptcy cases and proceedings

(a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11.

(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

APPENDIX F

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF INDIANA

Case#99-13425-13

Indianapolis, Indiana
February 29, 2000
9:43 a.m. O'clock

IN THE MATTER OF;)
)
LEE AND AMY TILL)
)
Debtors.)
)

**** Excerpt ****

TRANSCRIPT OF CONTINUED HEARINGS ON:
(1) TRUSTEE'S MOTION TO DISMISS;
(2) OBJECTION TO CONFIRMATION FILED BY SCS CREDIT CORP., AND DEBTOR'S RESPONSE FILED THERETO
BEFORE THE HONORABLE FRANK J. OTTE, J.U.S.B.C.

**** Excerpt ****

APPEARANCES:

For the Debtors:

EDWARD KOHAN, ESQ.
217 Southway Boulevard
Kokomo, IN 46502

For SCS Credit Corp.:

JOHN SMITH, ESQ.
214 W. Marion Street
Elkhart, IN 46516

For the Chapter 13 Trustee:

ROBERT BROTHERS, ESQ.
Office of Robert A. Brothers, Chapter 13 Trustee
151 N. Delaware Street, Suite 1400
Indianapolis, IN 46204

Electronic Sound Recording Operator: Cathy Ford

Proceedings Recorded by Electronic Sound
Recording Transcript Produced by Certified
Transcription Service

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[P. 9] In terms of what's out there now and the approaches being used in the appellate court system, I'm impressed mostly by the -- what appears to be a standard that possibly a majority of the courts are adopting, and that's the prime-plus standard that Judge Bayt used in his *Carson* decision -- decision back in 1998, and I think Judge Metz subsequently followed it, and that's simply computing the prime interest rate as of petition date -- not as of confirmation date, but a nice, easy, out-front date, easy for all to compute -- date of petition. When you're ready to file it you compute the prime and then add what historically these cases are treating as a one to three per cent additional risk factor in order to give the creditors some buffer against possible loss.

In this case, in *Carson* Judge Bayt pegged it at prime plus one and a half and adopted that as his future standard for

all automobile interest rates that would come before him, and I think Judge Metz has followed that. That has added simplicity in our ability to run our office, and it's something that is readily computable and I think works quite effectively.

The courts have noted that you don't really have to reward the creditor with a higher interest rate over and above what it would have to pay to borrow money, and I know the creditor before the Court today is seeking what I perceive to be kind of its standard lending rate or market rate of 21 per cent, but this is just one creditor with this rate. Many of [P. 10] our other lenders are substantially lower, so there appears to be little certainty when a debtor or debtor's counsel would attempt to prepare a petition as to what one would have to offer. Do you have to come up with a 21 per cent for this creditor, or can you go down the road -- ?

For instance, the other day I noticed Hubler Dodge, down at 3800 South East Street or South Madison, their market rate was absolutely zero finance charge, and they were doing that as part of a promotion, but that was their rate. So their -- in essence, with them you can walk into their dealership, compute the price of a brand new vehicle, divide it by 36 or 48 or 60 months, and that's your payment.

Without a standard other than market rate -- or with the market rate standard that I think the creditor seeks and I'd ask this Court to adopt, you're always going to be playing with something slipping and sliding around that the average counsel wouldn't be able to compute it. The prime plus is easily ascertainable on a daily basis, and it wouldn't work in a way to engage this Court in sort of a, what I think is a

frustrating search for what might be non-existent markets or non-existent similar loans that you would be dealing with.

The parties all look to the *Koopman's* case, Judge -it's the Seventh Circuit Chapter 12 case that came down some time ago to treat the interest factor that would be allowable. I really, probably for the first time -- I'd read *Koopman's* [P. 11] before but never gave it a hard read. I did it this morning, and I'm -- it's kind of amazing when you go through the ruling. They adopt the prime plus standard, yet within the same sentence state that the lender is entitled to its market rate of interest. You can't have it both ways. You simply can't. I think there must have been some confusion at that level.

At the close-out of *Koopman's*, though, I think one of the final lines that the Court, the Seventh Circuit level, said,

> "You simply have to read the cost of capital from newspaper tables, based upon actual transactions in competitive markets."

Well, I did that today. I pulled the newspaper and I looked at it, and the table I saw is prime. It's the only thing I could go by other than T-bill rates, which are lower, and I think probably no one has. Prime, as of today, for instance, is 8.75 per cent interest.

Now if you track the -- if you track the Judge Bayt decision in *Carson* you'd add one and a half points to that and you'd have a ten and a quarter loan, easily computable when you sit down and meet with the debtor and put together a plan and yet gives the creditors some hedge factor on its risk. I

think it's a good idea, and I think it's an appropriate standard to adopt.

The auto lender further has other built-in...

[P. 23] THE COURT: Well, you feel free when you want to, Mr. Brothers. Counsel may examine.

MR. KOHAN: Thank you.

DIRECT EXAMINATION

BY MR. KOHAN:

Q. Please state your name for the Court.

A. Steve Russell.

Q. And where are you employed?

A. I'm the Professor of Economics at IUPUI.

Q. Would you go through your employment history a little bit?

A. Yeah, I've had a -- got a Ph.D. from the University of Minnesota. I taught at the University of Georgia for four years. I worked as an economist in the research department of the Federal Reserve Bank of St. Louis for three years, and I've been at IUPUI for six or seven years.

Q. What are you currently teaching?

A. The course that I teach the most frequently is Money and Banking.

Q. Okay. Thank you. Let me ask you this generally, what's the purpose of the prime rate? Why do banks and other lending institutions use that as a benchmark in computing interest rates, or starting at least off on interest rates?

A. Well, the prime rate is a rate that banks charge on loans to their most credit-worthy corporate customers, and it's part of a uniform national market, so it's a uniform rate across the [P. 24] country. So it's easy to point out, you know, the rate on this particular class alone is going to be the same in California as in New York or anywhere else in the country, so it's a benchmark, a national benchmark rate.

Q. Okay. Does that generally take into account the change in the value of the dollar? Or maybe if you want to get into what this whole concept of the changing value of the dollar?

A. Yeah, there's three or four things in the prime rate that are also in any other market interest rate of varying degrees. There's an adjustment for the change in the purchasing power of the dollar, or the inflation rate. Right now that's probably two and a half per cent or so. There is an adjustment for the fact that something you referred to that people prefer dollars now to dollars later, and so a dollar now is a little more valuable than a dollar later, even if there is no risk that the dollar won't be repaid. And that -- that number right now is probably roughly three and a half per cent. That's the difference between the inflation rate and the interest rate on a very safe loan to the federal government, a Treasury bond, okay?

So that would take us up to roughly six per cent, which was the Treasury rate on comparable loans, I think, at the time of this bankruptcy filing. The prime rate was, at the time was closer to eight per cent, and that two per cent is mostly, I think, risk to some extent transactions costs. There [P. 25] is some risk on these loans, even though they're to pretty credit-worthy firms, because in most cases they're not secured, which makes them different from, say, a car loan.

Q. Mmhmm.

A. There's no explicit collateral on most of these loans.

Q. So generally, the loans that are secured, let's say you said car loans are -- have lower interest rates than unsecured, let's just say credit card loans?

A. Right. What matters is what the lender is likely to get in the event of a default, and obviously he's likely to get much more on a secured loan than on an unsecured loan. On an unsecured loan it's possible to get nothing, and often happens.

Q. So they get some of the collateral and at least get some of their costs back.

A. Right.

Q. Okay. What, in your opinion, generally speaking, what are some of the facts -- other factors that go into interest rate? You could look at prime rate, but obviously not if you want to use it as prime rate. What else is it -- what else -- what's the main factor that goes into -

A. Yeah, if you look at interest rates on loans, you know, that have rates above the prime interest rate, which most loans do, probably the single biggest determinant of the interest rate is the risk on the loan over and above the risk on one of these loans to a corporation that presumably is a very good [P. 26] credit risk. There is also an adjustment for the transactions costs of making a loan, which can include things like legal costs. I could include overhead for providing the facilities to have people come in and borrow, so there is a variety of different costs involved in making loans, and those are different, for different classes of loans, and so higher for some, lower for others.

Q. Let me ask you this: Based on what you've heard and what's been presented, would you feel that a nine and a half per cent interest rate is a reasonable interest rate for this -- for an auto creditor, given the present value of their claim?

A. "Yeah, I guess -- I would think that nine and a half was plenty. I looked at the interest rate, the current average interest rate in the United States on new car loans. Now this is a used car loan, so you might want to add a little bit to that rate, but it was roughly eight and a half per cent, so actually interest rates on car loans are pretty low. Again, the -- close to the prime rate because the security provided by the car kind of offsets the fact that these are loans to very credit-worthy firms.

Q. Mmhmm.

A. So the additional one and a half per cent, you know, in the prime plus one and a half, I guess you could interpret as an adjustment for the fact that the transactions costs of [p.

27] making small loans to people to buy cars are higher than the costs of making big loans to General Motors or whatever. And so it seems like a very reasonable rate. So with the understanding that the risk on making the loan is fairly limited because the borrowers are under the supervision of the court and are working with a plan that's supposed to be financially feasible, et cetera, et cetera.

MR. KOHAN: Okay. Thank you very much. I'm done, Your Honor.

THE COURT: Mr. Smith, cross-examination, sir.

MR. SMITH: Thank you, Your Honor.

CROSS-EXAMINATION

BY MR. SMITH:

Q. Sir, have you ever worked for a creditor?

A. I actually have worked for a commercial bank briefly, before I went to graduate school

Q. And when was that?

A. That was when I was an undergraduate -- would have been in the late 1970s, early 1980s.

Q. Okay, are you familiar with the particular credit criteria that any individual banks use in determining when to make a loan to particular customers or applicants?

A. Well, not in any degree of detail. I mean, I know the factors that are involved, but I wouldn't know how any particular creditor would assess those factors.

[P. 32]

A. Because the typical customers that we sell cars to have poor credit histories and are risky customers.

Q. Are you familiar with the credit history of the debtors and other relevant characteristics?

A. Yes.

Q. Is the credit history and the credit characteristics of the debtors similar or typical of the types of customers that Instant-Auto Finance typically sells to?

A. Yes.

Q. What was the rate of interest that Instant-Auto Finance charged the debtors when this vehicle was sold?

A. 21 per cent.

Q. What is the rate of interest typically charged by Instant-Auto Finance?

A. 21 per cent.

Q. Does Instant-Auto Finance ever sell vehicles on credit other than to employees for a rate of interest of less than 21 per cent?

A. No.

Q. Based on your job experience in the industry are you aware of the interest rate charged by other similar lenders in this area?

A. Yes.

Q. And what is -- what is that rate of interest?

A. 21 per cent.

[P. 33]

Q. How does Instant-Auto Finance view a credit applicant who appears to be a candidate for a Chapter 13 bankruptcy petition?

A. Negatively.

Q. Are you aware of how other lenders similar to Instant-Auto Finance view credit applicants who appears to be candidates for 6 Chapter 13 bankruptcy?

A. Negative as well.

Q. And would your answer be the same if I were to ask you how Instant-Auto Finance or other similar lenders view applicants -- credit applicants who are actually in a Chapter 13 proceeding?

A. Yes.

MR. SMITH: I have no further questions, Your Honor.

THE COURT: Cross-examination of this witness?

CROSS-EXAMINATION

BY MR. KOHAN:

Q. You decide whether or not to give credit to particular negative particular people, right?

A. Right.

Q. Do you actually decide on an interest rate? I mean I understand it's always 21 per cent. Is that something that you made the call, or does someone else make that call at 21 per cent?

A. Someone else makes that call.

Q. So is it set by someone higher up in the company? Is that [P. 34] it?

A. Yes.

Q. So you really -- you don't know where they come up with that 21 per cent. It's just something they told you you charge people with bad credit.

A. I believe it's what the market will bear.

Q. Well -- but I mean you don't know how they determined that 21 per cent interest, is that correct?

A. Correct.

Q. Okay. You may have heard these arguments, a lot of references to present value. Do you understand what present value means in the bankruptcy sense or the economic sense?

A. No.

MR. KOHAN: Okay. Thank you.

MR. SMITH: No further questions, Your Honor.

THE COURT: You may step down, sir. Any further witnesses?

MR. SMITH: Yes. One more, Your Honor. Neil Bird.

NEIL BIRD, LENDER'S WITNESS, DULY SWORN

THE COURT: All right, sir. Please have a seat, state your name for the record.

THE WITNESS: My name is Neil Bird.

THE COURT: Counsel may examine.

MR. SMITH: Thank you, Your Honor.

DIRECT EXAMINATION

[P. 35]

BY MR. SMITH:

Q. What's your address; Mr. Bird?

A. 1722 Bader Avenue, South Bend, Indiana.

Q. And where are you currently employed?

A. SCS Credit Corp.

Q. And how long have you been employed there?

A. Four years.

Q. And what is your job title or your position there?

A. I'm the general manager of SCS.

Q. Does that involve overseeing collections of accounts?

A. Yes, it does.

Q. Where did you work before you were employed by SCS Credit Corp.?

A. Teachers' Credit Union.

Q. How long did you work there?

A. Nine years.

Q. You've heard some of the testimony today about prime and non-prime lending markets. How would you characterize SCS Credit Corp.?

A. We're a non-prime lender.

Q. How would you characterize Teachers' Credit Union, your employer of nine years before coming to work for SCS Credit Corp.?

A They were a prime lender.

Q. Does SCS take assignment of retail installment contracts [P. 36] from Instant-Auto Finance?

A. Yes, we do.

Q. And is that what happened in this particular case with the debtors --

A. Yes.

Q. -- and the contract that they signed?

A. Yes, it is.

Q. Are you familiar with the credit history and the credit characteristics of the debtor?

A. Yes.

Q. Are the credit history and credit characteristics of the debtors similar to other customers that SCS Credit Corp. takes assignment of --

A. Yes, is it.

Q -- on a retail installment contract basis?

A. Yes.

Q. What is the rate of interest on the retail installment contract that SCS takes assignment of?

A. Twenty-one per cent.

Q. Is that always the case with non-employers? Are there ever any exceptions made?

A. No, there's not.

Q. And what is the rate of interest that the debtors agreed to on this particular retail installment contract?

A. Twenty-one per cent.

[P. 37]

Q. How does SCS Credit Corp. view Chapter 13 bankruptcy petitions?

A. We do not like them.

Q. Why not?

A. Because usually we don't get paid the full plan for the vehicle.

Q. Okay. Is there any delay in receiving the money?

A. Yes, there is.

Q. Do -- do Chapter 13 debtors ever enter into a plan and then SCS Credit Corp. actually never receives any distributions under the plan for one reason or another?

A. Yes, that's correct.

Q. Do you know how other non-prime lenders view Chapter 13 bankruptcy petitions, both with respect to potential applicants or customers that they already have on their books when a Chapter 13 petition is filed?

A. They're the same as SCS. They do not like them.

MR. SMITH: Okay. I have no further questions.

THE COURT: Cross.

CROSS-EXAMINATION

BY MR. KOHAN:

Q. Do you con -- do you set interest rates for SCS? Do you--

A. No, I do not.

Q. -- do you control that? So again, that comes from the higher-up in the company, I take it -...

APPENDIX G

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

Case#99-13425-FJO-13
CHAPTER 13

[Filed January 19, 2000]

IN RE:Till, Lee Madison	)
312-78-7180	)
Till, Amy Helen	)
313-98-1051	)
	)

AMENDED CHAPTER 13 PLAN

TO THE HONORABLE UNITED STATES BANKRUPTCY JUDGE OF SAID COURT:

COMES NOW, Lee Madison Till and Amy Helen Till, Debtor(s) herein, and proposes the following plan under Chapter 13 of the Bankruptcy Code:

1. The debts of DEBTOR(S) duly proved and allowed to shall be paid to the holder thereof in accordance with the provisions of Chapter 13 of the Bankruptcy Code and this Plan:

2. The future earnings of DEBTOR(S) are submitted to the supervision and control of this Court, and DEBTOR(S) shall pay tot he TRUSTEE a sum of $740.00 per month in weekly installments by voluntary wage assignment by separate ORDER of the Court in an estimated amount of $170.77 and continuing for a total plan term of 36 months unless this Court approves an extension of the term not beyond 60 months from the date of filing the Petition herein.

3. From the payments received, the TRUSTEE will make disbursements in the following order:

(a). *Administrative Expenses:* The TRUSTEE shall FIRST pay the expenses as prescribed by the Court, for administering of this plan. Expenses do not include an attorney fee as the DEBTORS qualify for benefits under their Pre Paid Legal Services Program and no fees are charged for services in this case.

(b) *Priority Claims:* All Claims entitled to Priority under Section 507 of the Bankruptcy Code will be paid as follows:

Creditor: Internal Revenue Service
Claim Amount Estimated: $2,582.00
Interest: Statutory interest

(c). *Secured Claims:* Secured creditors, whose claims are duly and timely filed, approved and allowed will be treated as follows:

(1). *Valuation of Collateral:* The Creditors listed below have a claim secured by a lien on the collateral shown

and the claim of each such creditor is secured to the extent of the fair market value of such property. The value of such creditor's interest is such collateral is as set forth herein below and such fair market value of such property is binding as to each creditor. The purpose of this plan provision and the valuation is to clearly provide that once Debtor(s) have paid such fair market value through the TRUSTEE, the lien of each such secured creditor shall be deemed invalid and satisfied, and at such time, each creditor shall immediately execute and deliver any and all necessary documents to effectuate release of such lien and delivery of an unencumbered title to the Debtor(s). Each creditor herein shall retain its lien existing prior to the commencement of this case only to the extent of the value of its collateral to secure payment as outlined herein.

Creditor: Ace Financial
Claim Amount: $8,500.00
Interest: 9.5%

Creditor: Heilig-Meyers Furniture
Claim Amount: $50.00
Interest: 0%

Creditor: Radio Shack Credit Card Plan
Claim Amount: $75.00
Interest: 0%

Creditor: SCS Credit Corporation
Claim Amount: $4,225.00
Interest: 9.5%

(2). *Payment of Secured Claims:* Secured claims duly and timely filed and allowed will be paid current with all above classes of creditors pro rata.

(3). *Void Liens:* The secured creditors listed below hold a non-purchase money, non-posserory security interest on Debtor(s) exempt property. Their liens will be voided pursuant to 11 U.S.C. section 522(0 and their claim treated as unsecured and paid pursuant to paragraph (e) below:

Creditor: Heilig-Meyers Furniture Co.

(d) *Special Class:* The following specially classified claims shall be paid as follows:

NONE

NONE

(e) *Unsecured Creditors:* Unsecured claims will be paid by the TRUSTEE after payments of the aforementioned categories, to creditors who have duly and timely filed and proved their claim, with the same having been allowed by the Court, with such payments or dividends to be paid in lieu of the debt and in satisfaction of the debts of such creditors.

(f) No interest, penalty or additional charge shall be allowed on any account subsequent to the filing of the petition herein, except that interest shall be allowed on claims to fully secured creditors in accordance with 11 U.S.C. section 506(b).

4. Debtors shall pay direct the following debts outside the Plan:

Creditor: Rent-A-Center
Claim: $6,600.00

5. The following secured claims are not dealt with in the Debtor(s) Plan, therefore, upon confirmation of the Debtor(s) Chapter 13 Plan, the automatic Stay Provisions of 11 U.S.C. section 362 will be terminated and annulled with respect to each of the following claims:

NONE

The remaining portion of the debt (deficiency) of the above listed creditors under paragraph 5 shall be disallowed as a claim as the collateral is being surrendered in full satisfaction of the debt.

(6). All executory contracts of the Debtor(s) will be assumed unless specifically rejected herein. The following executory contracts and/or leases are assumed or rejected as indicated below:

Creditor: Bradford Run Apartments
Contract is: Rejected

Creditor: DMA Enterprise
Contract is: Assumed

Creditor: Maple Crest Apartments
Contract is: Rejected

Creditor: Rent-A-Center
Contract is: Assumed

(7). Upon confirmation of this plan, title of the property of the estate shall vest in the Debtor(s).

(8). The funding of this plan will include federal tax refunds if due in an amount not to exceed one half of said refund over the base amount of $500 allowed to the debtor(s) as a cushion amount yearly if said is received. The debtor agrees to provide a copy of the tax return filed in the year immediately following the confirmation of this Plan by April 15th of the said following year and each year thereafter during the term of this Plan.

Date: 13 Jan 00 Debtor: /s/Amy H. Till

Date: 13 Jan 00 Debtor: /s/ Lee Till

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